1031-B | Y4.Sm1:Su6/2

97th Congress
2d Session | COMMITTEE PRINT

ORIGINAL

COMPLETED

INTERIM SUMMARY OF ACTIVITIES

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES
NINETY-SEVENTH CONGRESS
SECOND SESSION

Y4.Sm1:Su 6/2

SEPTEMBER 1982

Printed for the use of the Committee on Small Business

U.S. GOVERNMENT PRINTING OFFICE
97-911 O WASHINGTON : 1982

COMMITTEE ON SMALL BUSINESS

PARREN J. MITCHELL, Maryland, *Chairman*

NEAL SMITH, Iowa
JOSEPH P. ADDABBO, New York
HENRY B. GONZALEZ, Texas
JOHN J. LaFALCE, New York
BERKLEY BEDELL, Iowa
HENRY J. NOWAK, New York
THOMAS A. LUKEN, Ohio
ANDY IRELAND, Florida
IKE SKELTON, Missouri
BILLY LEE EVANS, Georgia
CHARLES W. STENHOLM, Texas
ROMANO L. MAZZOLI, Kentucky
NICHOLAS MAVROULES, Massachusetts
CHARLES HATCHER, Georgia
RON WYDEN, Oregon
DENNIS E. ECKART, Ohio
BYRON L. DORGAN, North Dakota
GUS SAVAGE, Illinois
BUDDY ROEMER, Louisiana
JOHN G. FARY, Illinois

JOSEPH M. McDADE, Pennsylvania
SILVIO O. CONTE, Massachusetts
J. WILLIAM STANTON, Ohio
WILLIAM S. BROOMFIELD, Michigan
DAN MARRIOTT, Utah
LYLE WILLIAMS, Ohio
OLYMPIA J. SNOWE, Maine
DANIEL B. CRANE, Illinois
JOHN HILER, Indiana
DAVID MICHAEL STATON, West Virginia
VIN WEBER, Minnesota
HAL DAUB, Nebraska
CHRISTOPHER H. SMITH, New Jersey
ED WEBER, Ohio
DAVID DREIER, California
GUY V. MOLINARI, New York
MARK D. SILJANDER, Michigan

MAJOR L. CLARK III, *Staff Director*
THOMAS G. POWERS, *General Counsel*
LOIS LIBERTY, *Publications Specialist*
RAYMOND S. WITTIG, *Minority Counsel*

LETTER OF TRANSMITTAL

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, D.C., September 24, 1982.

ALL MEMBERS,
Committee on Small Business,
House of Representatives,
Washington, D.C.

DEAR COLLEAGUE: I am pleased to submit this "Interim Summary of Activities" covering the 97th Congress to date.

Due to the extensive activities affecting small businesses it is deemed that this document will be of assistance to all Members of the Committee and Congress as a reference outlining the activities of the Committee on Small Business during the 97th Congress.

Best wishes,

PARREN J. MITCHELL,
Chairman, Committee on Small Business.

Blank Page

Blank Page

CONTENTS

	Page
I. Introduction	1
Number and jurisdiction of subcommittees	1
Disposition of legislation referred	2
II. Committee legislation enacted	3
Small business section of Budget Reconciliation Act, Public Law 97-35	3
The Small Business Innovation Development Act of 1982, Public Law 97-219	4
III. Committee legislation reported	6
8(a) Army Pilot Program extension	6
Second Omnibus Bill of the 97th Congress—H.R. 6086 (H. Rept. 97-564)	6
IV. Full committee activities	10
Full Committee hearings	10
Tax issues considered by Small Business Committee	12
Disaster assistance	15
SBA disaster loan program changes since March 1981	16
Procurement	18
Prompt Payment Act, Public Law 97-177	18
Retainage	19
Uniform Federal procurement system	20
Department of Defense small business policies	21
Regular 8(a) program	21
V. Investigations of meat marketing and food manufacturing industries	23
Legislation	24
VI. Economic review of small business problems	26

HEARINGS

VII. Subcommittee on SBA and SBIC Authority, Minority Enterprise and General Small Business Problems	28
VIII. Subcommittee on General Oversight	32
IX. Subcommittee on Antitrust and Restraint of Trade Activities Affecting Small Business	36
X. Subcommittee on Energy, Environment, and Safety Issues Affecting Small Business	44
XI. Subcommittee on Tax, Access to Equity Capital and Business Opportunities	47
XII. Subcommittee on Export Opportunities and Special Small Business Problems	57
XIII. Hearings and meetings held by the Committee on Small Business and Subcommittees, 97th Congress	59

INTERIM SUMMARY OF ACTIVITIES

I.—INTRODUCTION

This is the first report in the 97th Congress on the activities of the standing Committee on Small Business. The Committee is bipartisan recognition that the Nation's small business people represent a major segment of our business population and our Nation's strength. This Committee, continuing its vital oversight responsibilities, serves as the advocate and spokesman for small business as well as the hub for small business legislation. The year-to-date activities have been so extensive as to warrant this interim report and review of those activities so that those interested in small business matters may be more fully informed.

NUMBER AND JURISDICTION OF SUBCOMMITTEES

During the 97th Congress the Committee has been organized into six standing subcommittees each having jurisdiction including the following:

I. SBA AND SBIC AUTHORITY, MINORITY ENTERPRISE AND GENERAL SMALL BUSINESS PROBLEMS

Access to SBA services.
Illegal activities affecting small business.
Minority enterprise.
SBA and SBIC authorizations.

II. GENERAL OVERSIGHT

General oversight of activities of Government agencies and legislation affecting small business.
Postal Service.
Procurement.

III. ANTITRUST AND RESTRAINT OF TRADE ACTIVITIES AFFECTING SMALL BUSINESS

Anticompetitive activities affecting small business.
Federal Trade Commission and antitrust activities.
Robinson-Patman Act.
Sherman and Clayton Acts.
Unassigned Regulatory Agency activities.

IV. ENERGY, ENVIRONMENT, AND SAFETY ISSUES AFFECTING SMALL BUSINESS

Department of Energy and related agencies.
Energy allocations, marketing, etc.
Energy Research and Development contracts.

Impact of pollution laws and EPA rules.
Marketing of petroleum products.
Occupational Safety and Health Administration.
Science boards and commissions.
Tennessee Valley Authority.

V. TAX, ACCESS TO EQUITY CAPITAL AND BUSINESS OPPORTUNITIES

Access to equity capital.
Banking practices.
EDA.
Franchising practicies.
HUD policies affecting small business.
Impact of tax policies on small business.
Job creation.
SEC handling of ventures.

VI. EXPORT OPPORTUNITIES AND SPECIAL SMALL BUSINESS PROBLEMS

Export opportunities for small business.
Reduction of unnecessary paperwork.
Regulatory Flexibility Act.
Various communications matters affecting small business.
Various Federal regulatory policies and programs affecting small business.
Various transportation matters affecting small business.

DISPOSITION OF LEGISLATION REFERRED

The Committee on Small Business, as of September 24 of the Second Session, has completed action on the majority of legislation referred.

A total of 64 House bills and one House Concurrent Resolution were referred to this Committee. Fifty were considered and enacted into law, passed the House or were otherwise disposed of; and fourteen await further action.

The Committee's Small Business Innovation Act of 1981, H.R. 4326, was enacted on July 22, 1982, as Public Law 97-219.

In following the Committee's policy of consolidating related measures into omnibus bills whenever possible, numerous measures were combined into omnibus legislation and resulted in enactment of one (H.R. 2998) as part of last year's Budget Reconciliation Act (Public Law 97-35), and House passage of the second omnibus measure (H.R. 6086) now awaiting conference.

In addition, a Committee initiative was enacted through legislation also pending at other House Committees: Public Law 97-177, the Prompt Payment Act.

II.—Committee Legislation Enacted

SMALL BUSINESS SECTION OF BUDGET RECONCILIATION ACT PUBLIC LAW 97-35

The small business section of the Omnibus Reconciliation Act of 1981 (H.R. 3982, Title XIX) provided for a 32-percent reduction in SBA business lending for fiscal year 1982 and for substantial increases in interest rates for both regular business loans and disaster loans.

In addition, the reconciliation measure included the provisions of the Committee's first omnibus bill, H.R. 2998, which provided for a consolidation of several categorical programs into the 7(a) regular business loan program and unified most interest rates and loan terms, but retained separate funding levels for some of these programs. Those involved include 7(e) trade adjustment, 7(h) handicapped assistance, 7(i) economic opportunity, 7(l) energy conservation and 501 and 502 State and local development company loans. The only exemption from the new unified interest rate will involve loans to handicapped individuals or to organizations for the handicapped. These will remain at 3 percent.

Interest rates for SBA business loans are now set at the cost of money to the Federal Government plus up to 1 percent. Currently this figure is 14¾ percent.

Congress also legislated a mandatory 90-percent guarantee on SBA financings of $100,000 or less and from 70 percent to 90 percent on financings exceeding $100,000. The 1-percent guarantee fee which banks may pass on to the customer was retained. Interest-only payments which had been approved by the House were dropped. The terms for SBA loans were extended to a maximum of 25 years, plus such time as is necessary to acquire real estate or for construction, conversion, or expansion of facilities.

On SBA disaster lending, Congress extended provisions in the law requiring a "credit elsewhere" test to both business and home disaster applicants only to determine appropriate interest rates. Businesses unable to obtain credit elsewhere would be eligible for disaster loans at not more than 8 percent. Creditworthy businesses would be eligible for money at the prevailing market rate—currently running about 15 percent—for a maximum term of three years. Business disaster borrowers would be eligible for loans of up to 85 percent of the uninsured loss incurred.

Disaster loan rates for homeowners unable to obtain credit elsewhere would be half the cost of money to the Government, plus 1 percent, up to a maximum level of 8 percent. Creditworthy home disaster borrowers would be eligible for disaster assistance at full cost of money to the Government plus up to 1 percent, currently 14¾ percent.

97-911 0 - 82 - 2

Existing law concerning agricultural producers' eligibility for SBA assistance remains unchanged.

The economic injury loan program will remain, but will now include a statutory credit elsewhere test. The former SBA nonphysical disaster loan programs were consolidated into a new "Government impact" loan program, but the new program was not funded.

THE SMALL BUSINESS INNOVATION DEVELOPMENT ACT OF 1982, PUBLIC LAW 97-219

H.R. 4326, The Small Business Innovation Development Act of 1982, signed by the President on July 22, requires all government agencies with extra-mural Research and Development (R&D) budgets in excess of $100 million to establish Small Business Innovation Research programs (SBIR's) patterned after the highly successful pilot program instituted at the National Science Foundation (NSF) in response to congressional mandate nearly six years ago. Qualifying agencies are required to expend a fixed percentage of their extra-mural R&D budgets for this competitive small business program to be phased in over a four-year period as follows: .2 percent in 1983; .6 percent in 1984; 1 percent in 1985; and 1.25 percent in 1986. The Department of Defense is given an additional year because of budget size: .1 percent in 1983; .3 percent in 1984; .5 percent in 1985; 1 percent in 1986; and 1.25 percent in 1987. Agencies with smaller R&D budgets of at least $20 million are to set annual goals for small business involvement in Federal R&D efforts.

Based on the 1982 R&D budget which amounts to nearly $40 billion, 75 percent of which is "extra-mural," nine Federal agencies will qualify for SBIR programs during fiscal year 1983. These agencies are: DoD, NASA, DoE, HHS (NIH), NSF, Agriculture, Transportation, EPA, and the Nuclear Regulatory Commission. The Department of the Interior is likely to qualify the following year. The Congressional Budget Office estimates SBIR program levels ranging from $50 million in 1983 to $465 million in 1987.

Qualifying agencies will actively solicit small business proposals in broad categories of research in a three-phase program. Phase I consists of grants to determine the merits and feasibility of innovative ideas. In Phase II, somewhat larger grants would be available to pursue those ideas which show exceptional promise, with some consideration being given to commercialization potential. Phase III requires private capital funding to pursue commercial application, or, where appropriate, follow-on production contracts for Government use.

The pilot program established at NSF in 1977 has been extremely successful in stimulating innovation, generating business growth, and increasing employment in project award winners. This highly competitive program has won the admiration and respect of both the business and scientific communities. Of modest size, only $5 million, the NSF SBIR program has demonstrated a return on investment of nearly four to one and growing. Employment in participating firms has doubled. Extension of this program to other R&D intensive agencies is expected to bring returns to the economy in new technologies and business formations without increase in the Federal budget.

This bipartisan legislation is a response to numerous studies showing that small firm innovation far exceeds technological breakthroughs by large firms and that the cost per innovation is far less. Yet despite a disproportionately large contribution, small businesses have received only a tiny portion of the Federal R&D dollar. Redirecting a percentage of the Federal R&D effort to these small but efficient and highly innovative performers will be a more effective use of public funds.

H.R. 4326 is similar to Title I of H.R. 5607, reported out of the Small Business Committee during the 96th Congress after five days of hearings. H.R. 5607 was not acted upon by the House before final adjournment. This legislation was included in the top six priority recommendations from a list of 60 recommendations by the 1980 White House Conference on Small Business.

Several small business innovation bills were introduced in the 97th Congress and were considered by the House Small Business Subcommittee on General Oversight in hearings on September 15, 1981. H.R. 4326 was amended to consolidate the best features of these bills and was unanimously adopted and favorably reported by the Subcommittee on October 7, 1981. On October 22, 1981, the full Committee ordered H.R. 4326 to be favorably reported by unanimous vote (H. Rept. 97–349, Part I).

Sequential referral was requested and granted to six other House Committees: Science and Technology; Energy and Commerce; Armed Services; Veterans' Affairs; Foreign Affairs; and the Permanent Select Committee on Intelligence. Chief opponents of the legislation were from the bureaucracy and from large research-oriented universities and large research-related industries. Supporters included the U.S. Chamber of Commerce, the National Federation of Independent Businesses (NFIB), Small Business United, the Independent Business Association of Washington, the Small Business Association of New England (SBANE), the Mid-Continental Small Business United, the Coalition of Small and Independent Business Associations (COSIBA), the National Small Business Association (NSB), past administrators of SBA, SBA's first Chief Counsel for Advocacy and its current Chief Counsel, among others.

Based on a compromise adopted by the Small Business Committee on May 18, 1982, an amendment to H.R. 4326 in the nature of a substitute consisting of the text of a clean bill, H.R. 6587, was considered during House debate on June 17, 22, and 23. Amendments to exempt DoD, NIH, and Agriculture from the program were soundly defeated. The Committee agreed to accept amendments to exempt the Intelligence agencies, Atomic Energy Defense Programs, and AID international research centers and grants to foreign governments from the base against which the percentages are applied.

H.R. 4326 was passed by the House 353 to 57 on June 23, 1982. The text of H.R. 4326 was substituted for the text of S. 881 which had passed the Senate 90–0 in December of 1981, and on June 27, the Senate agreed to concur in the House amendments. The bill was signed in a White House ceremony on July 22.

The Small Business Administration has been given responsibility to monitor independently the SBIR programs and has 120 days in which to issue policy directives.

III.—Committee Legislation Reported

8(a) Army Pilot Program Extension

On October 6, 1981, the Committee met and ordered reported H.R. 4500, a bill to extend the 8(a) Army Pilot Program until September 30, 1983. The bill also includes extension of the Surety Bond Waiver Program through fiscal year 1983 (H. Rept. 97-304).

The 8(a) Army Pilot Program was included in Public Law 95-507, now more than three years old. It is designed to provide assistance to economically and socially disadvantaged small businesses in contracting areas not commonly reserved for the regular 8(a) program. The procurement contracts for these SBA-certified businesses are to be in specialized technological, manufacturing, and construction areas. After enactment of the law including the pilot procurement program, President Carter chose the Department of the Army as the agency to be designated for the program.

As provided in the original law, the pilot program expired on September 30, 1981. An extension was recommended because both SBA and the Department of the Army moved slowly in implementing the program. It was nearly 18 months into the two-year program before the Federal agencies agreed upon guidelines for the program. The pilot program had been extended once before.

The surety bond waiver section of the bill is designed to help small businesses receive contracts through SBA's 8(a) Business Development Program. It would allow SBA to waive requirements that a firm be bonded if it is found that the firm cannot obtain the necessary bonding from a conventional surety bond company or through SBA's surety bond guarantee program. This program has also been slow to be implemented and to date, there have been no firms receiving the surety bond waiver.

The Subcommittee on SBA and SBIC Authority, Minority Enterprise and General Small Business Problems held hearings on H.R. 4500 in late September of 1981. Witnesses testifying included SBA Administrator Michael Cardenas; Henry Exchwege, Director, Community and Economic Development, General Accounting Office; and Al Harrell, President, HI-LO Industries, a firm participating in the program. The Committee reported H.R. 4500 on October 28, 1981. The bill passed the House November 17, 1981.

In further action, the provisions of H.R. 4500 were included as section 20 of H.R. 6086 (S. 1947), as passed the House June 8, 1982.

Second Omnibus Bill of the 97th Congress—H.R. 6086 (H. Rept. 97-564)

As passed the House on June 8, 1982, the main features of H.R. 6086 are as follows:

1. *Program Levels*—Section 1 would increase existing authorized program levels in 1983 and 1984 for MESBICs, SBICs and EOL guarantees as follows:

A. The existing authorization for MESBIC funding is $35 million per year in each of fiscal years 1982, 1983, and 1984. The administration has requested an increase in the level to $41 million each year. The bill would increase it to $41 million in 1983 and 1984.

B. The existing authorization for guarantees of debentures for SBICs is $160 million in each of fiscal years 1982, 1983, and 1984. The bill would increase it to $250 million in 1983 and 1984.

C. The existing authorization for economic opportunity loan guarantees is $60 million in each of fiscal years 1982, 1983, and 1984. The bill would increase it to $167 million in 1983 and 1984.

2. *Mandate Spending*—Under existing law the Small Business Act specifies the maximum amount of loan and guarantee assistance which may be made available but does not require any minimum. Section 2 of H.R. 6086 would require SBA to approve assistance in the maximum amounts permitted in appropriations acts unless there is a lack of qualified applicants for assistance.

This amendment expressly recognizes and permits changes by reprogramming requests if approved by the Appropriations Committees.

3. *Pollution Control Financing*—Under existing law SBA has taken the position that it need not approve guarantees under the Pollution Control Guarantees Program if the proceeds for the project are from tax-exempt revenue bonds. Section 3 of H.R. 6086 would expressly prohibit the administration from denying the guarantee because tax exempt financing is involved.

In addition, this amendment expressly makes the change applicable to those applications pending on January 1, 1982 or made after December 31, 1981.

4. *Surety Bonds*—In order to reduce budget levels, early in 1982 SBA limited surety bond guarantees to a maximum of $250,000 (instead of the statutory $1 million) and further limited the maximum amount to not more than 125 percent of the amount of the firm's highest previous successfully completed contract. As of April 1, 1982, SBA eliminated the $250,000 cap and increased the percentage limitation from 125 percent to 200 percent. Section 4 of H.R. 6086 would expressly prohibit SBA (or SBA upon instructions from OMB) from limiting the maximum amount of a bond below the statutory limit and from utilizing a percentage increase limitation except on a case-by-case basis. Although SBA may have eliminated most of the problem with its April 1 change, nonetheless it can just as easily reverse itself again. Therefore, the matter should be addressed in statute.

5. *Guaranteed Loan Interest Rates*—The Small Business Act does not have an expressed interest rate for the 7(a) guaranteed loan program. Therefore, under existing law SBA has used its discretion to set guaranteed loan interest rate maximums at the prevailing commercial prime rate plus 2¼ percent on loans with maturities of less than seven years and at prime plus 2¾ percent on loans with maturities of seven years or more. In 1981 the agency proposed eliminating the add-on, and this would have been disastrous for the program. SBA is not actively pursuing the proposed change, but its

National Advisory Council has recommended a new formula limit based on Treasury bills. Section 5 of H.R. 6086 would set the maximum rate at prime plus the percentages now in existence via regulation.

This amendment would freeze the existing "prime plus" formula until June 30, 1983 to permit full review of this matter.

6. *Record of Applicants*—SBA does not now keep a record of those who inquire about SBA assistance and thus is never in a position to give Congress a valid indication of program demand. Section 6 of H.R. 6086 would require SBA to keep a record of the names and addresses and amounts requested by loan applicants or those who inquire about loan availability.

7. *Small Business Committee Notification*—Section 7 of H.R. 6086 would codify the current generally-adhered to practice of SBA notifying the Small Business Committees before reprogramming any program levels and to require that SBA notify the Committees before implementing any reorganization.

8. *Technicals Regarding Loan Consolidation*—Last year's reconciliation bill did not update cross references to the individual separate loan programs which were consolidated into section 7(a). Sections 8 and 9 (a)-(c) of H.R. 6086 change the references.

9. *Labor Surplus Area Direct Loan Program*—Sections 10 and 11 of H.R. 6086 establish a new direct loan program directed toward areas of high unemployment, especially if the loan proceeds will be used for construction, renovation, or purchase of land, buildings, machinery, or equipment. Each SBA district office would receive an allocation of total direct loan funds based upon the amount of unemployment in the district.

10. *Labor Surplus Procurement*—Section 13 of H.R. 6086 would make certain technical amendments to existing legislative authority pertaining to the labor surplus area procurement set-aside program. In addition, re-enacting subsections (d), (e), and (f) of section 15 of the Small Business Act would promote a greater degree of uniformity in the Federal acquisition system by removing the existing prohibition against DoD participation in total labor surplus area set-asides.

11. *Notice of Federal Procurements*—Section 14 of H.R. 6086, which incorporates H.R. 5551, would establish minimum notice requirements for Federal procurements advertised in the *Commerce Business Daily:* Fifteen days between publication of the notice of issuance of the request for bids or proposals and an additional 30 days after such issuance and awarding of the contract.

12. *Technical Disaster Changes*—H.R. 6086 corrects technical errors regarding the disaster changes made by last year's reconciliation bill.

13. *Size Standards*—SBA maintains that promulgation of rules and regulations regarding size standards is not mandatory under the Administrative Procedure Act but they have voluntarily brought themselves under the act. Section 16 of H.R. 6086 would expressly mandate that any size standard changes be in accordance with the Administrative Procedure Act.

14. *MESBIC Financing*—The GAO originally issued an opinion that MESBIC's could use State or other Federal financing as part of their leverage to obtain SBA funds. A few MESBIC's relied on

this and were organized on this basis. Subsequently, the GAO reversed itself. Section 17 of H.R. 6086 would allow MESBIC's, which relied on the original GAO ruling prior to its revocation, to obtain SBA funding as permitted under the original ruling.

15. *Development Company Working Capital*—Under section 502 of the Small Business Investment Act of 1958, the use of financial assistance provided by SBA to development companies is restricted to land, capital improvements, and machinery needs of assisted small business concerns. Section 18 of the bill expands the permitted use of proceeds to include working capital.

16. *Source of Development Company Funds*—Guarantees on behalf of development companies under section 503 of the Small Business Investment Act of 1958 may be used to provide funding for up to one-half of project cost. SBA has refused guarantees if the non-SBA portion is partially or wholly funded by Industrial Revenue Bonds. Section 19 of the bill would prohibit SBA from using the source or nature of the other funds as a criteria of eligibility.

17. *8(a) Pilot Programs*—Both the 8(a) Procurement Pilot and Surety Bond Waiver Pilot Program extensions through fiscal year 1983 (as originally in H.R. 4500) were included in H.R. 6086 as section 20.

18. *Limitation on Use of SBA Loans*—H.R. 6086 amends the SBA's section 7(a) loan authority to prohibit financial assistance to benefit any applicant which performs abortions, engages in abortion research, promotes or recommends abortion, or provides abortion training.

In all events, promotion or training for abortion is not to be financed. However, if an applicant performs abortions or promotes or recommends abortion only in cases where the life of the mother would be endangered if the fetus were carried to term, such activities would not preclude SBA 7(a) assistance.

19. *Effective Date*—In order to comply with requirements of the Budget Act, H.R. 6086 is to be effective October 1, 1982.

IV.—Full Committee Activities

FULL COMMITTEE HEARINGS

Although Committee activities and hearings are divided into legislative and oversight areas, investigative matters are included within the oversight category and what begins as oversight/investigative frequently becomes legislative.

In an effort to keep the open line of communication for necessary legislation which the White House Conference established between the small business community and Congress, the Chairman began a series of quarterly meetings with the small business trade organizations. The meetings are proving to be an effective mechanism to bring the associations' direct presence to the Committee resulting in ideas for legislation, a feeling for the problems encountered in doing business with the Federal Government and reactions to the administration's tax changes. Most trade association representatives indicated that tax and credit problems are their top legislative priorities for the 97th Congress. More than 100 association officials from across the country attended these meetings. In the second meeting the Chairmen of the six House Small Business Subcommittees presented brief legislative reports.

Meetings have been held on February 23 and September 16, 1981. Field hearings were held in Los Angeles, July 7; Chicago, July 18; Phoenix, September 1, 1981; Atlanta, January 18; and Philadelphia, March 15, 1982, for those who could not travel to Washington to express their concerns. The Committee expects to continue these meetings to hear directly from small businesses and their representatives about the effects of current economic policies and about the problems they are encountering with the Federal Government.

The Committee's beginning schedule was monopolized by a series of hearings made necessary by the Reagan administration's budget request and program changes for the Small Business Administration, including a 32-percent reduction in loan guarantees and consolidation of previously categorical programs. (Hearings and markups were held March 12 and 18, June 2 and June 9, 1981.) These administration budget revisions affecting small business have required continuing investigations and hearings to date.

On April 7, 1981, the Committee held a hearing on the impact of the administration's economic, tax, and spending proposals on small business, and the Federal Reserve's future conduct of monetary policy.

In the last Congress the Committee conducted extensive hearings and issued a report on the effect that the Fed's policy has had on small business. High interest rates, while not considered in detail by delegates to the White House Conference on Small Business, have become a major factor in the dramatic increase in small business failures. Federal Reserve Board Vice Chairman Frederick

Schultz testified on the effect of Fed policy on the small business community. The Committee continued to address the problems of high interest rates and their effect on small business.

The Committee and the House Education and Labor Committee's Subcommittee on Labor Standards on April 29, 1981, held a joint hearing on "Economic Programs to Stimulate Employment in the Small Business Sector." The hearing explored ways in which wage subsidy incentives have worked in the past and how well suited they may be in the long term needs of American labor and industry. In addition, the effectiveness of these wage and subsidy programs compared to other employment and training programs proposed by the Reagan administration and the Congress were examined.

The Committee met on June 2 and 9, 1981, to consider the recommendations of the Subcommittee on SBA, SBIC Authority, Minority Enterprise and General Small Business Problems regarding H.R. 2998, the Loan Consolidation and Improvement Act of 1981. The purpose of the bill is threefold—to comply with budget reconciliation requirements; to minimize its adverse impact; and to assist small business. This legislation was enacted as part of the First Session's reconciliation measure, Public Law 97-35.

At its meeting of June 9, 1981, the full Committee considered necessary reconciliation measures, business and disaster loan consolidation and assistance and technical amendments to the Equal Access to Justice Act (although in the bill as reported the latter was deleted in conference). On June 16, 1981, H.R. 2998, as amended, was reported (see House Report 97-150). The administration rejected H.R. 2998 in favor of the Gramm/Latta substitute in the omnibus reconciliation measure. For further action see Committee Legislation Enacted.

The series of five Committee field hearings thus far this Congress, collectively known as "Small and Minority Business in the Decade of the 80's," has examined the 1982 budget cuts which are having a considerable impact on many beneficial programs administered by SBA. In addition, new regulations on the 8(a) minority business development program and guaranteed loan interest rates proposed by SBA raise serious concerns about the future of these vital programs. In previous field hearings, the Committee heard from witnesses involved in these Federal Government programs and has gained valuable insight into problems faced by small and minority business owners. Bringing the Committee into the field to meet directly with small business entrepreneurs highlights the commitment that the Congress has toward a healthy, vibrant small business sector and follows up on the White House Conference delegates' recommendations.

The Committee continued oversight of the SBA's proposed major revision in size standards first announced during the 96th Congress. The second proposed rule defining what is small for purposes of Government assistance was published for comment on May 3, 1982. Comments were due on August 2, 1982, and the proposal, as amended, will again be published for comment before being finalized.

97-911 O - 82 - 3

Extensive interest in SBA's Federal timber set-aside program resulted in a separate final regulation determining small business for purposes of this program.

Based on small business' particular needs for tax relief and the recommendations of the White House Conference on Small Business, the Chairman introduced H.R. 3930, the Small Business Tax Relief Act of 1981, to provide much-needed tax relief to the small business community. A more extensive analysis of these two initiatives is included under the section on tax issues affecting small business.

Further Committee action on H.R. 1139, a bill to amend Title 38, United States Code, to establish a business loan program for disabled veterans and veterans of the Vietnam Era, and for other purposes, referred jointly with the Committee on Veterans' Affairs, became unnecessary upon enactment of Public Law 97-72 whose title III accomplishes this 1981 objective.

On March 2 and 9, 1982, the Committee considered the administration's SBA budget request. The Committee sharply differed with the administration's budget requests, particularly insofar as eliminating SBA's direct loans, reducing SBA's pollution control equipment contract guarantees, reducing the amount of guaranteed loan authority and the amount of surety bond guarantee authority.

As a result of this hearing, the Committee also proposed as the new direct loan program for small firms located in labor surplus areas. This proposal is now contained in H.R. 6086 as reported by the Committee and as passed the House June 8, 1982.

TAX ISSUES CONSIDERED BY SMALL BUSINESS COMMITTEE

In conjunction with the Subcommittee on Tax, Access to Equity Capital and Business Opportunities, the Committee received testimony from many witnesses and associations regarding changes in the tax code which would be of benefit to small businesses. The Committee, whenever possible, introduced and supported legislation implementing the recommendations of the delegates to the White House Conference on Small Business which was held in January 1980. Five of the top seven recommendations of the delegates were changes in the tax code, confirming small businesses' belief that tax reform is necessary to their growth and success.

The Chairman introduced H.R. 3930, the Small Business Tax Relief Act of 1981, to provide much-needed tax relief to the small business community.

In a time of rising unemployment, high interest rates, and inflation, Congress should give special consideration to the problems of the small business community. This legislation addressed the broader needs of the small business community and was intended to: (1) Reduce corporate tax rates; (2) increase the amount of used equipment and machinery eligible for the investment tax credit; (3) increase the maximum number of shareholders in a subchapter S corporation from 15 to 25; (4) increase the estate tax exemption from approximately $175,000 to $300,000 and increase the gift tax exclusion from $3,000 per year to $10,000 per year.

The present corporation tax rate structure places a difficult tax burden on small businesses. Although a significant number of small businesses conduct business in the form of a sole proprietor-

ship or partnership, there are also many small businesses that use the corporate structure. Thus, the reduction of the corporate tax rates will benefit a significant number of these firms. There is currently a five-tiered corporate tax structure. The bill would establish a seven-tiered rate, in place of the present five tiers, and substantially reduce the tax burden on the first $200,000 of taxable income.

Many small businesses cannot afford to purchase new equipment and machinery and are forced to maintain a viable business with used equipment and machinery. This problem is compounded by the limit on the amount of used equipment and machinery eligible for the investment tax credit. This legislation, increasing the then-limit from $100,000 to $300,000, would benefit those small businesses that traditionally purchase used equipment. In addition, this provision enables the taxpayer to carryback and carryforward the amount of the investment made over the prescribed limit. Currently, section 48 of the Internal Revenue Code of 1954 unfairly discriminates against small business because only used equipment is subject to the limitation with respect to the 10-percent investment tax credit; new equipment is not limited. Moreover, the carryback and carryforward provisions are for taxpayers who purchase new equipment; however, no such provision exists for those who purchase used equipment or machinery. This legislation would eliminate this disparity between the purchasers of new and used equipment.

The present estate and gift tax provisions of the Internal Revenue Code inhibit the transfer of a family owned small business from one generation to the next. This legislation, raising the then-estate tax exemption from approximately $175,000 to $300,000, would provide relief for the family owned small business. In some instances, the heirs of a family owned business are forced to sell the business in order to pay the estate and inheritance taxes. An increasing number of family-held small businesses are forced to sell their businesses to large firms, thereby contributing to the growing trend of monopolies and greater concentration of businesses which undermines our free enterprise system. Increasing the estate tax exemption to $300,000 will relieve some of the estate and inheritance tax burden on the heirs of a family owned small business. H.R. 3930 also includes a provision to raise the gift tax exclusion from the then-limit of $3,000 to $10,000 per year. This would enable members of a family owned small business to have a valuable planning tool which will relieve some of the burdens of our estate tax system.

The subchapter S corporation came into existence in 1958 and was designed to allow small corporations which are essentially partnerships to enjoy the corporate form of organization without being made subject to the possible tax disadvantages of a corporation.

The advantage of a subchapter S corporation is that it allows the shareholders to pay income taxes and utilize corporate losses as if they were a partnership. It is becoming increasingly difficult for small businesses to obtain adequate financing due to high interest rates and other market forces. This legislation, increasing the maximum number of shareholders permitted to operate a sub-

chapter S corporation from the then-limit of 15 to 25, would alleviate some of the shareholders' problems and increase the appeal of the subchapter S corporation. Consequently, this provision would enable shareholders to pool their resources while simultaneously allowing for a greater distribution of the risks associated with the operation of a small business.

Many important provisions of H.R. 3930 were incorporated into the final tax relief measure adopted by the Congress in the First Session, the Economic Recovery Tax Act of 1981.

The Economic Recovery Tax Act of 1981 contains several provisions of special interest to the small business community ranging from a reduction of individual income tax rate to improved inventory accounting rules. Following is a brief outline of pertinent provisions of interest to small concerns.

1. *Individual Income Tax Rates Reduction*—A 5-percent reduction effective October 1, 1981, and additional 10 percent rate reductions on July 1, 1982, and July 1, 1983, giving an overall 25 percent reduction during a 33-month period. For those taxpayers who conduct business in the form of a sole proprietorship, partnership or subchapter S corporation, the rate reduction could result in substantial tax savings during the period. Also, beginning in 1985, the individual income tax brackets, the personal exemption and the zero bracket amount would be indexed to the consumer price index to offset the effects of inflation.

2. *Depreciation of Personal Property Used in a Trade or Business*—The main depreciation provision is generally referred to as "10–5–3," and enables a business to recover the cost of property in 15, 10, 5, or 3 years. The depreciation provisions also contain a direct expensing section which would permit the cost of property to be recovered by a single deduction for the year the property is placed in service. The bill would permit a taxpayer to expense a maximum of $5,000 in 1982 and 1983; $7,500 in 1984 and 1985; and $10,000 per year beginning in 1986. Taxpayers have the option to expense the maximum amount and to depreciate the remaining cost of the property by use of the "10–5–3" method.

3. *Investment Tax Credit*—An increase in the investment tax credit limit on used equipment from $100,000 to $125,000 in 1981 through 1984 and to $150,000 in 1985 and thereafter.

4. *Subchapter S Corporations*—An increase in the permissible number of subchapter S shareholders from 15 to 25 and permission for the creation of shareholder trusts under certain circumstances. This provision took effect January 1, 1982.

5. *Corporate Accumulated Earnings Credit*—An increase in the minimum accumulated earnings credit from $150,000 to $250,000, effective January 1, 1982.

6. *Business Inventory Rules*—Improvements in LIFO inventory rules to remove impediments to the use of LIFO by small business, effective January 1, 1982.

7. *Corporate Tax Reduction*—Reduction of the corporate tax rates for those corporations earning $50,000 or less as follows: Corporations earning from $0–$25,000 now paying 17 percent would pay 16 percent in 1982 and 15 percent in 1983; corporations earning from $25,001–$50,000 now paying 20 percent would pay 19 percent in 1982 and 18 percent in 1983.

8. *Estate and Gift Taxation*—An increase in the exemption from estate tax from $175,000 to $600,000 by 1987. A lowering of the maximum estate tax rates from 70 percent to 50 percent. An unlimited marital deduction provision which will mean that there will be no estate tax on bequests made to spouses. The gift tax exclusion has been increased from $3,000 to $10,000, effective January 1, 1982.

DISASTER ASSISTANCE

The Small Business Administration provides loan assistance to disaster victims, including homeowners, businesses, and nonprofit institutions. When disaster strikes it is important that damaged property be replaced or repaired and businesses be provided with adequate working capital for recovery as soon as possible. SBA disaster loans serve this purpose and minimize disruptions of jobs, business revenues, and taxes. In so doing, they play a vital role in restoring the economic health of a disaster-stricken community, often making the difference in the survival of businesses necessary to that recovery.

During the 97th Congress, major revisions were made in SBA's disaster loan program, both by statute and by regulation. These changes began early in 1981 when the administration took the following actions:

1. It withdrew a pending request for $780 million in supplemental disaster loan funds for SBA;

2. It suspended on March 10, 1981, the funding of all SBA disaster loans, and then published regulations on March 19, 1981, severely restricting eligibility, including: (a) the elimination of any eligibility for those businesses (including farmers) able to obtain alternative financing; (b) the limitation of the amount of the loan for those businesses remaining eligible to 60 percent of losses; (c) the imposition of a $100,000 ceiling on economic injury loans; and (d) the elimination of all funding for "nonphysical" disaster loans; and

3. It requested legislation which would have eliminated eligibility for both home and business disaster borrowers with personal resources or alternative sources of financing, and which would have raised interest rates on loans to those without alternative sources of financing to a formula rate representing the Government's cost of money plus 1 percent (approximately 15 percent).

These actions were taken without prior notice or consultation with the Committee. The March 19th rules changes were particularly inequitable, as they applied to all pending applications not yet acted upon, with the result that victims of the same disasters were treated differently. Although a large number of loan applications were pending when these restrictions were imposed, the administration refused to change its position, justifying it on the grounds of budgetary necessity.

Shortly after the administration took its unilateral actions, the congressional budget process forced the Committee to consider statutory changes in the disaster loan programs. The First Concurrent Budget Resolution of 1981 contained instructions requiring the Committee to effect major savings in the programs under its juris-

diction. It was impossible to comply with these requirements without affecting the disaster loan program.

The Committee considered various plans by which these savings could be made, including legislation which the administration had requested. As part of the Committee's examination of the potential effects of the proposed legislation, the staff conducted interviews with victims of recent disasters who had loans approved prior to the administration's rules changes. During April 1981, the staff took sworn depositions from 100 of these victims in Omaha and Grand Island, Nebr., and in San Diego, Vista, Burbank, and San Bernardino, Calif. The witnesses were asked to describe their experiences and what effect the administration's proposed legislation would have had on their recovery had it been in effect when they suffered their losses. Of the 93 physical disaster victims deposed (61 homeowners and 32 businesses), 82 percent indicated that they would not have been able to afford the proposed terms. All recipients of nonphysical disaster loans (both for regulatory compliance and displaced businesses) indicated that without such assistance they would have reduced employment or gone out of business.

On June 3, 1981, the Subcommittee on SBA and SBIC Authority, Minority Enterprise and General Small Business Problems held a hearing in which testimony similar to that taken in Nebraska and California was received from Baltimore disaster victims. After considering the information obtained in these field investigations, hearings, and other sources, the Committee met on June 9, 1981, and, after several close votes, recommended disaster program revisions which were accepted by the full House on June 26th as part of the Omnibus Reconciliation Act of 1981. After further compromise with the Senate, which had basically approved the administration's request, a final plan was approved in Title XIX of Public Law 97-35 on August 13, 1981.

The major revisions made in SBA's disaster loan program by Public Law 97-35 are summarized below together with regulatory revisions made by the administration. In addition to these revisions, Public Law 97-35 provided for the disposition of business loan applications affected by the administration's March 19, 1981 regulations.

SBA DISASTER LOAN PROGRAM CHANGES SINCE MARCH 1981

A. Statutory changes made by Public Law 97-35, effective for disasters commencing on or after August 13, 1981.

(1) Public Law 97-35 imposes a "credit elsewhere" test to determine the interest rate on disaster loans to repair or replace damaged homes and personal property.

Prior legislation treated all home disaster borrowers alike, regardless of their ability to secure alternative financing.

(2) Public Law 97-35 increased the interest rate on all home and personal property disaster loans. Those able to obtain alternative financing pay a formula rate relating to the Government's cost of borrowing plus 1 percent. This rate fluctuates and has been as high as 16 percent. As of July 1, 1982, the rate is 14¾ percent. Those unable to obtain alternative financing pay one-half the formula rate, 7⅜ percent as of July 1, 1982.

Prior legislation provided for a 3-percent interest rate on the first $55,000 of any disaster home loan.

(3) Public Law 97-35 increased the interest rate on disaster loans to businesses unable to obtain alternative financing to a maximum of 8 percent.

Prior legislation provided for a 5-percent rate for businesses in this category.

(4) Public Law 97-35 changed the interest rate on disaster loans to businesses able to obtain credit elsewhere to the commercial "prime" rate in effect on the day the disaster commenced.

Prior legislation provided that businesses in this category would pay a formula rate relating to the Government's cost of borrowing.

(5) Public Law 97-35 limits the term of loans to businesses able to obtain alternative financing to 3 years, except to avoid a hardship.

Prior legislation provided for a 3-year "graduation" review. If the business was able to obtain alternative financing at that time, it was required to do so. If not, the business could keep its Government loan which would be reviewed again every 2 years for graduation.

(6) Public Law 97-35 limits the amount of eligibility on all business disaster loans to 85 percent of physical losses.

Prior legislation allowed loans to cover 100 percent of physical losses.

(7) Public Law 97-35 rewrote SBA's eight "nonphysical" economic injury loan programs into a single comprehensive "Government impact" loan program to help small businesses cope with the effects of Government regulations or decisions. However, no funding of this program is currently authorized.

Prior legislation provided for nonphysical disaster loans designed to help small businesses overcome economic injury due to a variety of circumstances including, but not limited to, Government regulations and decisions.

B. Regulatory changes made by SBA, effective March 19, 1981.

(1) Regulations adopted March 19, 1981, changed the criteria by which an actual disaster declaration is made, increasing the amount of damage necessary before SBA disaster assistance can be made available. The new criteria require that either:

(a) 25 homes or businesses must have suffered a 40-percent uninsured loss; or

(b) 3 businesses must have suffered a 40-percent uninsured loss and as a result 25 percent of the work force in the community will be unemployed for at least 90 days.

Under prior regulations, a disaster was of such magnitude as to trigger SBA's disaster program if it met any of the following three criteria:

(a) 25 homes or 5 businesses, or a combination of 25, suffered 25 percent uninsured losses;

(b) 3 businesses suffered 25 percent uninsured losses and as a result 25 percent of the work force in the community would be unemployed for at least 90 days; or

(c) 200 homes or 40 businesses, or a combination of 200, suffered any loss.

(2) The March 19, 1981, regulations also suspended all disaster assistance to any business deemed able to obtain alternative financing and limited remaining business disaster loans to 60 percent of actual losses. However, these regulatory provisions were overturned by Public Law 97–35.

C. Regulatory changes made by SBA, effective for all disasters commencing on or after December 18, 1981, make ineligible for disaster assistance any damages to secondary homes and their contents. Also made ineligible for such assistance were boats, vehicles, and airplanes used primarily for recreation or relaxation.

Under prior regulations, disaster assistance could be provided to repair or replace such property.

It is clear that the present terms of SBA's disaster programs are more restrictive than they ever have been, and the Committee has been monitoring closely the effects of the revisions made necessary by the budget process. On June 8, 1982, the Committee held field hearings in San Francisco and Santa Cruz, Calif. to hear from victims of severe flooding and mudslides and public officials from the affected areas about their experiences with SBA's program. On June 19, 1982, the staff also conducted interviews with flood victims in Ft. Wayne, Ind. These three locations were selected because of the severity of the disaster damage and because they were among the first major disasters to be declared in which the disaster program revisions of Public Law 97–35 were in effect.

Witnesses indicated that the new program terms were, in many cases, causing hardships, much as a substantial majority of the 1981 witnesses in California, Nebraska, and Maryland predicted they would. In addition, preliminary data appear to indicate that the percentage of disaster loan applications which are declined, withdrawn, or remain unclosed, is increasing.

The Committee will continue to watch this situation closely and, subject to the constraints of the budget process, will do everything possible to ensure that the effectiveness of the disaster loan program is not further compromised.

PROCUREMENT

Prompt Payment Act, Public Law 97–177

The Federal Government processes 30 million invoices each year from roughly 75,000 individual contractors. Approximately 90 percent of the primary commercial products and services procured by the Federal Government are purchased from small dealers, distributors, manufacturers, and service-related firms.

Small businesses maintain competition in the market place by accepting smaller profit margins than large firms and by employing new technologies and procedures that increase productivity and, therefore, lower costs. If a sufficient number of small firms forego conducting business with the Federal Government, Federal procurement costs for goods and services will increase, ultimately at the expense of the American taxpaying public.

Before passage of Public Law 97–177, there was no statutory mandate requiring that the Federal Government pay its bills on time. While accepted commercial practice calls for payment within 30 days of invoice receipt, or the imposition of an interest penalty,

the Federal Government has not always conformed to this standard.

The Prompt Payment Act, signed into law May 21, 1982, requires that Federal agencies pay interest on overdue payments to businesses for property or services. To assist the Government in avoiding interest payments, the act requires that Government contracts stipulate a payment due date. If a contract lacks such a date, the 30-day commercial standard will apply, except for meats and perishable fruits and vegetables (which are already subject to a shorter period by statute). The rate of interest is to be pegged to that determined by the Secretary of the Treasury for payment under section 12 of the Contract Disputes Act. An agency must pay any interest penalty from the appropriation for its operating funds. An agency may take advantage of an early payment discount only if payment is made within the time specified by the business. Each agency must report annually to Congress concerning any interest payments incurred.

While the Prompt Payment Act was not reported by the House Small Business Committee, this Committee has had similar legislation before it (H.R. 3474 and H.R. 5075). Many times small concerns have testified before the Committee about the Government's tardy payment practices. Further, many members of this Committee were consponsors of bills on this subject, and all supported passage of the bill, H.R. 4709, when it reached the House floor.

The Committee believes that the passage of H.R. 4709 is a positive step indicating to the small business community a determination to put the U.S. Government on a businesslike basis. Paying bills on time, and paying penalties on overdue accounts, are common business practices which the Federal Government should adopt.

Retainage

In response to the beleagured contracting industry, the Chairman introduced H.R. 5022, to eliminate retainage for small business concerns on Federal Government contracts.

Retainage is the practice of withholding a percentage of the contractor's earned payment pending satisfactory completion of all required contractual work. Generally, when contractual work is performed for the Federal Government, the Government retains a portion of the prime contractor's payment and the prime contractor, in turn, retains a portion of its subcontractors' payment. Amounts to be retained are withheld from progress payments made periodically to the contractor by the procuring agency as work progresses on the contract. Present regulations provide that there shall be retained 10 percent of the estimated amount of such progress payments until final completion and acceptance of the contract work. However, the contracting officer has discretionary authority in this matter.

Under provisions of H.R. 5022, when authorized, no retainage is to be withheld from payments made for satisfactory contract progress; in addition, no retainage whatsoever is to be withheld from progress payments to small concerns which have furnished an adequate performance bond, as determined by the contracting officer.

Testifying at the May 5, 1982, hearing in favor of H.R. 5022 were national associations representing hundreds of thousands of members employing millions of Americans.

This hearing clearly establishes that the practice of retainage in today's business climate has outlived its usefulness, is a deterrent to vigorous competition in the construction industry, and causes unnecessary costs to Government. There are many reasons for ending this outmoded practice.

Retainage, in effect, is antithetical to the established Government policy of providing small businesses with necessary financing if they are otherwise qualified to perform Government contracts. The need for financial assistance should not be construed as a handicap to any contractor, if the contractor is otherwise reliable, competent, and responsible.

Enactment of the Small Business Contract Payment Procedures Act would put more than $4 billion directly into the hands of the private sector, available for business growth and job creation.

Because the administration's proposal for a Uniform Procurement System does not deal directly with the retainage question and, most probably, will not be enacted this Congress, it is hoped that the Government Operations Committee will take immediate action to hold hearings and report legislation to assist small concerns in overcoming the retainage problem.

Uniform Federal procurement system

Public Law 96-83 ("The Office of Federal Procurement Policy Act Amendments of 1979"), requires that OFPP develop a comprehensive and uniform procurement system for use by Federal agencies. On October 30, 1981, OFPP provided Congress its first proposal for a procurement system, a procurement management system as well as draft model procurement legislation.

On April 30, 1982, the administration transmitted its final proposal in the form of three draft bills, none of which has yet been introduced. These three bills, along with Executive Order 12352 issued by President Reagan on March 17, are the administration's comprehensive program for procurement reform. Congress is considering these legislative proposals essential for the accomplishment of the important and far-reaching reforms proposed. These reforms could result in savings upwards of $9 billion annually and renewed public confidence in the Federal procurement process.

In its hearings and in meetings with OFPP and small business groups, the Committee has always stressed that the Congress must keep in mind certain specific problems during any consideration of model procurement legislation. These include: (1) The disappointing performance of the Federal agencies in expanding the opportunities for small business, evidenced by the small business share of Federal procurement showing no appreciable growth in recent years; (2) how bid sets and specifications were very often unavailable to small businesses despite the enactment of Public Law 95-507 which mandates their availability; (3) how inadequate time is allowed from the time of publication of bid notice to bid opening date; (4) the increasing number of sole source procurements; (5) how small businesses are often excluded from bidding for Government contracts due to the lack of specifications and data which the

Government owns but has failed to obtain from the original contractors; (6) how Government change orders and design errors impose unnecessary and often devastating financial hardships upon small business; (7) how agency requirements for bidder "prequalification" are increasingly utilized to discriminate against small business; (8) late payment on Government contracts; (9) the practice of retainage; (10) Research and Development set-asides; and (11) preaward survey and audits being too costly for Government and small concerns.

The Committee will closely monitor the proposed laws and regulations for the new Federal Procurement System on behalf of its small business constituency.

Department of Defense small business policies

The Committee challenged a policy gaining momentum in the Department of Defense which would have excluded small and disadvantaged businesses from competing for Defense base service contracts.

On March 12, 1982, Chairman Mitchell wrote Deputy Secretary of Defense Frank Carlucci about the increasing use of single, multifunction "umbrella" base support contracts, questioning DoD's move to consolidate base support services into a single contract which only the largest firms are capable of performing. The result feared is that small and small disadvantaged businesses will be squeezed out by a few large firms, with a further erosion of competition for service contracts. Congressman Joseph P. Addabbo, a member of the Committee, also wrote the individual services in opposition to the use of umbrella contracts.

As a result, DoD reversed direction and decided that future solicitations, unless there are overriding national security considerations, will be packaged so as not to preclude performance by small and small disadvantaged concerns as prime contractors. This action, if implemented adequately by the individual services, should assure small and minority firms that they will receive a fair share of Federal service contract work. The Committee will be monitoring the situation to be sure that DoD follows through with its directive.

Regular 8(a) program

During the 97th Congress, the Commitee has been concerned about the lack of opportunity for minority firms in the section 8(a) Procurement Program.

Public Law 96–481, approved October 21, 1980, contains certain provisions which require SBA to establish a fixed period of time for every participant concerned, either to enter or remain in the section 8(a) program. Specifically, this legislation requires current participants in the program and new applicants to submit a business plan listing targets and objectives aimed at correcting the economic impairment which, in part, qualified the firm for the program, and a date for graduation from the program. The legislation further provided that the graduation date be fixed by SBA after negotiation with the program participant, that the date could be extended by SBA upon request of the 8(a) contractor, and that the date for existing 8(a) concerns would be fixed no later than April 21, 1982.

Although SBA has issued regulations implementing this legislation and has met the statutory deadline for establishing fixed program termination dates for existing participants, the Committee is very concerned about the inaction at SBA in response to recent 8(a) program size rulings made by the General Accounting Office and the Federal Courts. SBA's inaction may result in certain 8(a) firms in the program being denied contracts because they have grown larger prior to their projected graduation date. Both this Committee and the House Committee on Appropriations are concerned that SBA is unfairly counting the gross receipts or employment attributable to 8(a) contracts, and terminating a firm for being "other than small" based on that determination. Since 8(a) contracts are sources of temporary and remedial assistance, and since a firm terminated for being large will not receive such assistance, the firm will automatically become small as soon as it is terminated, and will suffer from many of the problems that were the basis for its initial admission into the program. Accordingly, SBA should develop economic criteria of competitive viability against which an 8(a) firms' progress or lack of progress can be based. In addition, any determination that an 8(a) firm is "other than small" ought not be based, in full or in part, on gross receipts or employment attributable to 8(a) contracts.

On August 17, 1982 the SBA published in the Federal Register an Interim Emergency Rule providing an altenative size standard for 8(a) firms. Since the emergency rule will, by its terms, expire in 180 days, the basic problem of how to measure the size a firm participating in the program is likely to repeat itself in the future.

The factors affecting national brand-private label price spreads, changes in prices over time and the amount of innovative activity; factors considered will include economies of scale, capacity utilization, market share held by private label and generic products, and the size and specialization of companies manufacturing private label and generic products.

The future organization of food manufacturing industries—given present trends and economic forces—and the expected role of large and small companies, the impact on consumers and labor, and the appropriate policy measures that could be considered to alter the above scenario.

The results of this analysis are expected during the 98th Congress.

V.—Investigations of Meat Marketing and Food Manufacturing Industries

(1) Staff report on the systematic downward bias in live cattle futures

In order to provide information on the role of commodity futures trading and its effects on small business, the Committee staff conducted an analysis of large (reporting) trader data, provided upon Committee request in accordance with section 8(e) of the Commodity Exchange Act by the Commodity Futures Trading Commission, for the live and feeder cattle futures markets of the Chicago Mercantile Exchange.

In accordance with section 8(a) of the Commodity Exchange Act, the staff report presented the results of the analysis in a form which did not reveal information about individual traders.

The report came to the following conclusions and recommendations:

A systematic trading technique which predicts certain live cattle futures price drops with 100-percent accuracy was discovered. This phenomenon means there is a large amount of short selling (relative to buying) entering the marketplace on a reoccurring, predictable basis. Available evidence indicates such short selling is generally coming from commercial feedlots, grain companies which own or have an interest in commercial feedlots, officers of these companies, officers of futures commission merchants and certain large farmers and speculators. The technique's predictive success implies that some cattle futures traders are aware of and taking advantage of the phenomenon discussed in this report. Since such knowledge can be used to profit from futures transactions to the obvious disadvantage of traders not in possession of this knowledge, it was recommended that the contents of the report be made public.

Based on the economic theory of efficient markets, the existence of the phenomenon described in the report provides strong evidence that the live cattle futures market is not operating as an efficient price discovery mechanism and that this market is operating with a consistent, systematic, perfectly predictable downward bias. Such a conclusion means the live cattle futures market is not fulfilling its economic purpose of providing a hedging vehicle (equally) to all traders.

Evidence indicated that the predictable drops in live cattle futures prices are not reflective of fundamental supply-demand.

As a hedging mechanism, the live cattle futures market is providing hedging opportunities only to those cattle feeders with the lowest per unit costs[1] and not to cattle feeders in general.

---

[1] Generally, these are lots feeding in excess of 30,000 head per year.

97-911 O - 82 - 3

Best Available Copy

A group of 32 large traders with correlated daily net trading activity and/or common business affiliations is a major force in the live (and feeder) cattle futures market and this group displayed a net daily trading pattern indicative of knowledge of the observed bias in prices.

Making the results of the report public should result in live cattle futures traders arbitrating the observed phenomenon out of existence. To the extent this occurs, the live cattle futures market would not only offer hedging opportunities to Corn Belt cattle feeders,[2] but also not offer hedging opportunities to large (least cost) commercial cattle fedders. In such an environment, the live cattle futures market would serve no economic purpose.

LEGISLATION

As a result of Committee studies of the live cattle futures market, Congressman Neal Smith introduced legislation (H.R. 5917) to deal with documented problems in cattle futures. The bill, which awaits action before the Committee on Agriculture, requires a producer referendum as a condition of designation of cattle futures markets.

Other legislation dealing with agriculture marketing problems included: H.R. 5956 to amend the Commodity Exchange Act to require public disclosure of grain export sales, by Congressman Neal Smith, referred to the Committee on Agriculture which took no action; H.R. 626 to repeal the 1976 official standards for grades of carcass beef, by Congressman Neal Smith, referred to the Committee on Agriculture which took no action; H.R. 630 to clarify the eligibility of certain small businesses for loans under the Small Business Act, and to aid, protect, and preserve small businesses in meat production and marketing, by Congressman Neal Smith, referred jointly to the Committees on Agriculture and Small Business, which took no action; and H.R. 631 to amend the Small Business Act to assist and protect small businesses against unreasonable use of economic power by major meatpacking companies, by Congressman Neal Smith, referred jointly to the Committees on Agriculture and Small Business, which took no action.

(9) Committee study of food manufacturing industries

Under the direction of Chairman Mitchell, the Committee staff began an analysis of food manufacturing industries in the United States to determine:

The trends in the structure of these industries and the relative importance of small and large companies.

The critical factors affecting the ability of small companies to survive and compete effectively.

The extent to which national brand food manufacturers are also engaged in the manufacture of private, controlled, and generic label products, the trends in this regard, and the impact of "dual branding" on competition in food manufacturing.

---

[2] See "An Assessment of the Performance of the Chicago Mercantile Exchange Live Cattle Contract as a Hedging Vehicle for Cattle Feeders," staff study, Committee on Small Business, U.S. House of Representatives, 96th Congress, 2d Session.

Best Available Copy

The factors affecting national brand-private label price spreads, changes in prices over time and the amount of innovative activity; factors considered will include economies of scale, capacity utilization, market share held by private label and generic products, and the size and specialization of companies manufacturing private label and generic products.

The future organization of food manufacturing industries—given present trends and economic forces—and the expected role of large and small companies, the impact on consumers and labor, and the appropriate policy measures that could be considered to alter the above scenario.

The results of this analysis are expected during the 98th Congress.

VI.—Economic Review of Small Business Problems

The House Committee on Small Business and its constituent subcommittees provide an ongoing review and summary of the economic impact on small businesses of legislation and Federal Government policy decisions. The reviews include a wide range of issues of importance to the small business community. Following is a partial listing:

Economic Outlook: The Economic Outlook is a bimonthly issue brief summarizing the major econometric forecasts and analyzing the impact of economic changes on small businesses.

The most recent report points out that:

(1) Small businesses continue to pay interest rates 10–12 percentage points above the rate of inflation—two to three times more than the historic average range of 3–5 percentage points from 1960 to 1978.

(2) Businesses in general and small businesses in particular are in their worst liquidity positions in postwar history.

(3) Testimony before Congressman John LaFalce's Subcommittee on General Oversight revealed that 10 percent of the 2,000 largest corporations and 15 percent or more of smaller businesses are "at risk" of failing.

(4) Small businesses in interest-sensitive sectors; e.g., housing and related businesses, durable goods retailers, automobile retailers, and agriculture, are particularly hard hit by the recession and high interest rates.

(5) Small businessess are being pushed out of short-term bank credit markets by large firms who are unwilling to commit themselves to pay historically high interest rates in the long-term corporate bond market. Small loans from banks (under $500,000) accounted for 35 percent of bank loans in February 1980 but only 12.2 percent in May 1982.

(6) High interest rates, the recession, and poor liquidity positions of businesses have resulted in the highest rate of business failures (as measured by Dun & Bradstreet) since 1933. Business failures recorded by D&B in the first 30 weeks of 1982 totaled 13,557—45 percent higher than a similar period in 1981 and more than double the 1980 level.

Small Businesses' Share of the Tax Reduction: An issue brief on small businesses' share of the cut reveals that small businesses[1] will receive a smaller than fair share of the general business tax reductions.

Small corporations constitute over 97 percent of all corporations, take over 19 percent of depreciation, and pay over 20 percent of corporate business taxes but can expect about 12–13 percent of the

[1] Small businesses are defined as those with less than $5 million in total assets in 1978 or, adjusting for inflation, $6.84 million in assets in 1982.

corporate share of business tax reductions (excluding safe harbor leasing).

Small businesses received about 0.3 percent (three-tenths of 1 percent) of the benefits from safe-harbor leasing in 1981. As a higher percent of smaller businesses tend to have low profits or no profits in any given year, the inability to take advantage of safe-harbor leasing puts them at a disadvantage relative to large firms.

All small businesses, including all sole proprietorships, all partnerships, and all small corporations will receive about 26 percent of the general business tax reductions. By way of contrast, small businesses generate over 43 percent of net business income, comprise 99 percent of all businesses, and pay 32 percent of business taxes.

An unknown portion of the small business share of the tax reduction will go to investment shelters in the form of proprietorships and partnerships rather than to active small businesses.

The fact that small businesses tend to pay higher rates of interest reduces small businesses' ability to invest relative to large businesses and reduces their potential share of the tax cut.

Historically high real interest rates, brought about a combination of tight monetary policy and massive deficits for the foreseeable future, have hit small businesses particularly hard, reducing small business investment and their portion of the tax reduction.

A higher percent of total taxes paid by small businesses is in the form of "fixed" taxes; i.e., those taxes which do not depend on the level of profits. Therefore, as profits fall, the tax burden of small businesses declines less than for large businesses.

Small businesses tend to be more labor intensive or land intensive (farming) than large businesses. Taxes on both land and labor have risen in recent years while the tax on capital has been sharply reduced and in some cases is negative (i.e., amounts to a subsidy for using capital). In the long-run, subsidizing the use of capital while taxing both land and labor will lower the efficiency with which resources are used in the American economy and lower the rate of growth of total factor productivity.

Business Failures: A preliminary report on Government policy and business failures has found a strong relationship between real interest rates (nominal rates minus the rate of inflation) and business failures. The analysis of the relationship between Government policy and small businesses economic health is continuing.

Monetary Policy: A series of hearings on the impact of current monetary and fiscal policies have been held by various subcommittees and are described under their activities.

HEARINGS

VII.—Subcommittee on SBA and SBIC Authority, Minority Enterprise and General Small Business Problems

The Subcommittee held a hearing on April 7, 1981, on the administration's proposed changes in SBA lending authority: H.R. 2998, the Loan Consolidation and Improvement Act of 1981. The bill was marked up on May 19, 1981.

An amended bill was reported unanimously from the Subcommittee on May 20th. As reported, the bill consolidated several categorical programs into the regular 7(a) business loan program, provided new terms for 7(a) business loans, authorized new funding levels for fiscal year 1983 and fiscal year 1984 and required SBA to compile information for the Congress on the default rate of business loans, refinancings, and extensions.

The Subcommittee began a series of hearings on the Small Business Administration's section 8(a) Procurement Program for small and disadvantaged businesses on May 21, 1981. Subsequent hearings were held on June 4 and June 10, 1981. The hearings were held to examine new SBA policies on 8(a) program size standards and certification requirements and the agency's new interim and proposed program regulations.

At the first hearings, SBA's Administrator Michael Cardenas emphasized the Administration's support for the 8(a) program despite new regulations issued which would dramatically curtail participation by minority businesses, and pending legislation to terminate the program.

The second hearing on the program brought together 8(a) contractors and trade associations testifying in support of the business development program. These hearings highlighted all aspects of the program so that it can be strengthened to better serve the minority business community.

The Subcommittee held a hearing on June 3, 1981, on H.R. 2997, and on SBA's disaster loan program. The Administration had proposed extensive changes in the disaster loan programs including restrictions on home disaster lending to persons who could not obtain credit elsewhere. Substantially higher interest rates were also proposed. Prior to the hearing, business disaster lending had already been administratively limited to 60 percent of actual net loss and ony to firms unable to obtain credit elsewhere. Nonphysical disaster loans were to be eliminated under the Administration's proposal.

The Subcommittee reviewed legislation extending SBA's 8(a) Pilot Procurement Program through September 1983 at a September 22, 1981 hearing.

On September 28, 1981, the Subcommittee met to consider H.R. 4500, legislation to extend both the SBA/Army 8(a) Pilot Procure-

ment Program and the SBA Surety Bond Waiver Program through September 30, 1983. Both administration and public witnesses participated. The 8(a) Army-Pilot Program was enacted as a part of Public Law 95-507 and is designed to provide assistance to economically and socially disadvantaged small businesses in high technology fields. The procurement contracts for these SBA-certified businesses are to be specialized technological, manufacturing, and construction areas.

Subsequent consideration was at the full Committee level. The bill was marked up and ordered reported on October 6, 1981 (H. Rept. 97-304).

On November 12, 1981, the Subcommittee held a hearing on the Department of Interior's regulatory enforcement of affirmative action for minority businesses in outer continental shelf leasing activities. Subsequently, the Department indicated that affirmative action regulations of OCS leasing activities would be forthcoming.

On September 23, 1981, the Subcommittee began a series of hearings to determine if local small and minority businesses ought to be a part of the cable television dialog, particularly in large urban areas. Also, the Subcommittee sought to determine if local small and minority businesses are being involved in the cable television industry and whether or not they are getting a fair share of contract and subcontracting opportunities.

During the Subcommittee's previous hearings, it was noted that increased concentration in media ownership due to the high financial cost of developing cable television has precluded many small and minority businesses from successfully entering the field.

There are more than 13 million small and minority businesses in this country. Many of these are in franchising operations. Cable television is a franchise business. Based on the findings of the September 23d hearing, the Subcommittee held an additional hearing on October 13, 1981, to determine if local small and minority firms are getting the opportunities to share in the ownership, service, and construction of cable television systems in cities such as Washington, D.C.; Detroit; Philadelphia; New York; Chicago; Cleveland; Los Angeles; St. Louis; etc.

The third and final hearing on November 4, 1981, was to determine if large majority cable systems can provide better cable services than the local independent small or minority-owned cable operator. Additionally, the Subcommittee's hearing was to determine how the more than 13 million local independent small and minority businesses in this country could be included in ownership, construction, and servicing of local cable TV systems. A committee report is forthcoming.

On February 25, 1982, the Subcommittee held hearings on the Reagan budget request for SBA for fiscal year 1983.

Hearings focused on why the small business community is experiencing one of its most drastic down cycles. In 1981 there were 17,000 business failures, the second highest level since World War II. The number of business failures for the first six weeks of 1982 was 2,560. If this failure rate continues through 1982, there will be approximately 22,000 failures by year's end. The highest number of business failures ever recorded by Dun & Bradstreet was 31,822 in 1932. While small business owners are hoping for an early upturn

in the economy, a continuing high deficit and prime interest rate are rapidly dimming such hope.

The administration's request was found to be counter-productive to the needs of the small business community. The administration should be providing more loan and management assistance, not less. Under the administration's proposal, the direct loan program would be eliminated and the guaranteed lending authority would be decreased to a level of $2.4 billion.

Other programs would be similarly reduced, with surety bond guarantees cut 23 percent from the currently authorized level and pollution control bond guarantees reduced 40 percent from their current level.

Minority business programs would also be cut. Although the administration has included $410 million in guaranteed loan authority for minorities, banks are simply unwilling to obligate this much to minority firms. They have never done so and will not do so in these hard economic times.

On April 28 and 29, 1982, the Subcommittee held hearings on two bills: H.R. 5551, which basically would require a 45-day lead time for Federal procurements between publication of notice of a pending procurement and issuance of the contract; and H.R. 6086, an omnibus bill which changes certain SBA program levels, requires that SBA fully utilize its programs and keep a record of applicants, prohibits SBA from refusing to issue guarantees on pollution bonds simply because the project involves an industrial revenue bond, prohibits SBA from arbitrarily refusing to approve surety bond guarantees on contracts eligible under statutory provisions, codifies existing regulations on interest rates on guaranteed loans, and requires the Small Business Administration to follow the Administrative Procedure Act if it revises its size standards. In addition, H.R. 6086 would direct the limited amount of direct loans to areas of high unemployment.

These two bills and other pending SBA and SBIC legislative authorizations were combined into the second omnibus bill of this Congress, H.R. 6086, and forwarded to the full Committee, which subsequently reported the measure (H. Rept. 97-564).

On June 16, 1982, the Subcommittee held a hearing on the administration's Small and Minority Enterprise Development Programs. This hearing focused on the Small Business Administration's 8(a) business development program and its small business subcontracting procurement programs. Programs at the Department of Commerce's Minority Business Development Agency were also examined.

The hearing examined concerns that, notwithstanding the vast contribution small and minority businesses are making to this economy, the Administration, under the guise of budgetary restraints and program efficiency, is moving in a direction that is counterproductive to the needs of the small and minority business concern.

The hearing gave the new leadership of SBA under Administrator Sanders an opportunity to put forward its position on necessary assistance for the small and minority business community.

Finally, the Minority Business Development Agency (MBDA), which has a key role to play in assisting minority businesses to

penetrate financial and contracting market areas, was also present to explain its new policy direction to achieve these goals.

The hearing gave direction to MBDA and SBA as to the right course in their agency missions to promote the growth and viability of the small and minority business community.

On May 5, 1982, the Subcommittee held a hearing on the problem of retainage in Federal procurement. The Chairman has introduced legislation, H.R. 5022, to eliminate retainage for small business concerns on Federal Government contracts.

Retainage is the practice of withholding a percentage of the contractor's earned payment pending satisfactory completion of all required contractual work. Generally, when contractual work is performed for the Federal Government, the Government retains a portion of the prime contractor's payment and the prime contractor, in turn, retains a portion of its subcontractors payment. Amounts to be retained are withheld from progress payments made periodically to the contractor by the procuring agency as work progresses on the contract.

Under provisions of H.R. 5022, when authorized, no retainage is to be withheld from payments made for satisfactory contract progress; in addition, no retainage whatsoever is to be withheld from progress payments to small concerns which have furnished an adequate performance bond, as determined by the contracting officer.

Testifying in favor of H.R. 5022 at the May 5 hearing were national associations representing hundreds of thousands of members employing millions of Americans.

This hearing clearly established that the practice of retainage in today's business climate has outlived its usefulness, is a deterrent to vigorous competition in the construction industry and causes unnecessary costs to Government.

VIII.—Subcommittee on General Oversight

Following are hearings conducted by the Subcommittee during the first session of the 97th Congress:

Impact of Reagan Economic Program on Small Business.—May 19, 1981.

The hearing heard from Prof. Francis Bator, a Harvard University economist; Prof. Robert Berney, a small business economist at Washington State University, Pullman, Wash.; and Norman Ture, Treasury Undersecretary for Tax and Fiscal Policy. The hearing focused on how small business would fare under the Reagan administration's economic program. Prof. Bator warned that the economy would slide into a deep and prolonged recession if the administration followed through on what he called its contradictory tight money and expansive fiscal policies. Prof. Berney focused on the deep deficits that were expected as a result of the loss of Federal tax revenues and the administration's failure to adopt real spending cuts. He warned that the deficits would keep interest rates high which, in turn, would seriously hurt small business. Dr. Ture said he was confident the the President's economic program would unleash the American economy and would ultimately help small business.

Small Business and the Federal Procurement System.—June 18, 23, and 25, 1981.

The 3-day hearing, which heard from Government, industry, and small business witnesses, focused on Government efforts to assure that small business received a fair opportunity to compete for Government contracts. Witnesses told of the difficulties encountered by small businesses in using the Federal procurement system and dealing with Government agencies, how increased use of small business could save the Government money, and the lack of understanding of small business' special needs and problems shown by the Reagan administration. The hearing was called to hear from the Office of Federal Procurement Policy, the Department of Defense, and the Small Business Administration how they planned to carry out the intent of Public Law 95–507 and the Labor Surplus Area and various small business set-aside programs.

Small Business Administration's Guaranteed Loan Policies.—July 30, 1981.

The hearing focused on the heavy burden of high interest rates on small businesses and ways to reduce the interest rates charged on SBA guaranteed business loans. The hearing heard from Ronald Piercy, a small businessman from Kansas City, Mo.; William Bolt, Vice Chairman, United Missouri Bank, Kansas City, Mo.; Paul E. Ruch, Executive Vice President, Marine Midland Bank, Buffalo, N.Y.; Jackie Kleiner, an Atlanta, Ga. lawyer challenging the validity of the prime rate; and Michael Cardenas, Administrator, Small Business Administration.

Small Business Innovation Development Act (H.R. 4326).—September 15, 1981.

The hearing laid the groundwork for House consideration of the Small Business Innovation Development Act (H.R. 4326). The Small Business Innovation Development Act provided for the establishment of Small Business Innovation Research programs in Federal agencies with research and development budgets exceeding $100 million a year. Witnesses included the National Council for Industrial Innovation, the Smaller Business Association of New England, the National Federation of Independent Business, the National Small Business Association, the American Association of Small Research Companies, the Association of American Universities, the Small Business Administration, Office of Science and Technology Policy, the Defense Department, National Aeronautics and Space Administration, the Department of Energy, the Department of Health and Human Services, and Dr. John Eastin, an inventor from Grant, Neb. The Subcommittee reported the bill unanimously on October 7, 1981. H.R. 4326 was unanimously reported by the full House Small Business Committee on October 22, 1981.

Insurance Agent Commission Deregulation.—September 21, 1981.

The hearing focused on H.R. 4497, the Insurance Sales Deregulation Act, which was introduced to repeal the portion of the McCarran-Ferguson Act which prohibits insurance agents from offering discounts on commissions. Witnesses included Ralph Nader; Susan Mitchell, Wisconsin Insurance Commissioner; insurance professors; and spokesmen for the insurance industry.

Worker Compensation Rate-Setting Reform.—February 18, 1982.

Two worker compensation insurance rate-setting practices which may be severely discriminating against our Nation's small businesses were examined by the Subcommittee. These practices appear to be so widespread and so deepseated that, notwithstanding recent efforts in a few States to reverse these practices, they continue to cost our Nation's business community in excess of $1 billion a year in inflated worker compensation premiums.

The two practices are: (1) The refusal by the insurance industry to submit worker compensation rates which reflect the billions of dollars of investment income earned by these insurers annually; and (2) the steadfast resistance by worker compensation insurers to switch from the present cartel-dominated fixed-rate system to one permitting open competitive rating.

Worker compensation insurance is a highly profitable line of business for the insurance industry. Annual premiums exceed $20 billion. However, worker compensation premiums frequently account for 10 percent or more of payroll costs for smaller labor-intensive firms. In some cases, small businesses pay as much as 20 percent of their payroll costs into worker compensation premiums.

The hearing examined the issue from the perspective of small business and explored ways to provide relief to small firms. The Subcommittee received written testimony from Michael Markman, the Minnesota Insurance Commissioner, who is a leader in efforts to reduce worker compensation premiums. It heard from William Johnston, Chairman of the Ohio Industrial Commission, and Spencer Kimball, Executive Director of the American Bar Foundation.

Best Available Copy

Both sides of the investment income and competitive rating issues were invited to the hearing to explore all aspects of the problem. Insurance industry representatives declined to appear.

The General Accounting Office was asked to investigate the rate making reforms discussed at the hearing.

Productivity.—March 23 and 24, 1982.

The hearings were held to learn more about the productivity improvement programs underway in the public and private sectors. Witnesses included officials from the U.S. Commerce Department, the U.S. Labor Department, the General Accounting Office, the Georgia Productivity Center, the Robot Institute of America, and the Japan Productivity Center. A major share of the testimony focused on the need for greatly increased productivity improvement efforts to serve the small business sector. Testimony concerning Japan's efforts to boost small business productivity was presented.

Impact on Small Business of Proposed Cuts in the Small Business Administration's Guaranteed Business Loan Program.—March 31, 1982.

At a time when small businesses find it hard to borrow money, the Reagan administration has made deep cuts in the Small Business Administration's guaranteed business loan program. Over the years, SBA guaranteed loans have been a safety net for small business. Thousands of small businessmen have found the SBA guarantee the only way they could receive a bank loan to start a new small business, tide a healthy small business over difficult times, and create thousands of new jobs. By fiscal year 1983, the Reagan administration will have cut SBA's guaranteed loan program almost in half, to $2.4 billion from $4.5 billion in fiscal year 1981.

The hearings focused on how small business today is being crowded out of bank lending, the traditional source of its capital; how guaranteed business loans have contributed to economic development and job creation; how the reductions in the guaranteed loan funds will hurt small business; and why the program is needed to make capital available to small business and contribute to an economic recovery.

Witnesses at the hearing included Joel Popkin, Joel Popkin & Co., Washington, D.C.; Professor Robert Berney, a small business economist at Washington State University, Pullman, Wash.; Harold Davis, President, Concentration Specialists, Inc., Andover, Mass.; Peter Howell, President, Down East Inc., Bridgton, Maine; Arthur Mitchell, Senior Vice President, Capital Bank & Trust Co., Baton Rouge, La.; and J. Knox McConnell, President, First National Bank of Keystone, Keystone, W. Va.

Current Business Failure Epidemic.—June 23, 1982.

More businesses are failing in 1982 than at any time since the Great Depression. The Dun & Bradstreet business failure rate for the first half of 1982 stood at 88 per 10,000 listed companies, the highest rate since 100 per 10,000 listed companies reported for 1933. These figures have serious implications. The U.S. economy needs a healthy, expanding small business sector if it is to recover from the current deep recession. Today's failures are almost all small businesses. The Dun & Bradstreet figures, which President Reagan's recent report on "The State of Small Business" calls a "valuable indicator of business distress," showed a 45-percent rise

Best Available Copy

in business failures from 1980 to 1981 and a 44-percent increase from the first half of 1981 to the first half of 1982.

The hearings brought together leading academic, industry, small business, and bankruptcy experts to discuss why there are so many business failures today and what the future holds. Witnesses included Dr. Edward I. Altman, a professor of finance at New York University and a leading expert in predicting business failures; Joseph W. Duncan, chief statistician of Dun & Bradstreet; Herbert Liebenson, President, National Small Business Association; Dean M. Gandy, U.S. Bankruptcy Judge, Dallas, Tex.; James T. Eichstaedt, U.S. Trustee, Los Angeles, Calif.; and William P. Westphal, Sr., U.S. Trustee, Minneapolis, Minn.

The Subcommittee was told that American business is experiencing its worst liquidity crisis since the Great Depression. At least 15 percent of the Nation's businesses are on the verge of failure, Dr. Altman testified, because they are so overwhelmed by high interest rates. The witnesses stated that the increase in failures cannot be attributed to the new Federal bankruptcy code that became effective in 1979. They warned that business failures would continue to rise sharply if interest rates continued at high levels, the recession persisted, and if economic policies were not changed to significantly lower interest rates and encourage a long, sustained recovery.

Section 503 Certified Development Company Program.—July 28, 1982.

The Subcommittee examined the Small Business Administration's Section 503 Certified Development Company Program as a model for local economic development and financial assistance to small business at affordable interest rates. The 503 program was established by Public Law 96–302 enacted on July 2, 1980. The program authorizes State and local development companies to issue debentures that carry a 100-percent SBA guarantee; to sell those debentures using SBA as their sales agent; and to use the proceeds to make low-interest, subordinated long-term loans to small businesses.

The 503 program is designed to stimulate the growth of viable small businesses through a public/private partnership. The program's purpose is to help local communities by encouraging the expansion of small businesses within a defined area of operation. The certified development companies provide long-term, fixed-asset financing to small businesses that would otherwise not be able to expand due to high interest rates or lack of bank financing.

The hearing explored how the 503 program is working and gave witnesses the opportunity to recommend changes in the program. The Subcommittee heard from John Sower, Executive Vice President, National Association of Development Companies; Aliceann Wohlbruck, Executive Director, National Association of Development Organizations; officials of local development companies; representatives from the banking industry; and James C. Sanders, Administrator, Small Business Administration.

IX.—Subcommittee on Antitrust and Restraint of Trade Activities Affecting Small Business

COMPETITION IN THE COMPUTER AND DATA PROCESSING INDUSTRY

Background

In an information-oriented business world, computer applications lie at the heart of the decision-making process. Rapid advances in commercial applications and technology have narrowed the distinctions between previously separated types of commercial activity. The once clear distinction between computing and communications has blurred considerably, and the Federal Communications Commission, the Judiciary, and the Congress have attempted for over a decade to determine what elements of these activities should be regulated as communications, and how they should be regulated.

The enormous growth in the computer and data processing field has spawned a large number of small and innovative firms in the last 15 years. The tremendous advances in services and technology over that time can be attributed to the vitality and creativity of an industry in an open and competitive market.

However, concern has arisen that this competitiveness may be threatened by the entry of large firms in regulated industries into the unregulated computer and data processing industry.

Summary of testimony

A hearing was held by the subcommittee on May 7, 1981, in Washington, D.C., to receive testimony from representatives of the computer and data processing industry. Witnesses who appeared and testified include: Association of Data Processing Service Organizations (ADAPSO), by David Chaffin and John Reardon; Computer Dealers and Lessors Association, by Ken Bouldin; Association of Computer Users, by Hillel Segal, President; Computer and Communications Industry Association, by Jack Biddle, President; Independent Data Communications Manufacturers Association, by Charles Johnson; and American Telephone and Telegraph, by Robert Allen, Vice President of Business Services.

The witnesses generally agreed that the industry was both growing rapidly and highly competitive. The concern of several witnesses was that the competitive nature of the industry would be damaged by the entry of regulated firms in the unregulated computer and data processing industry.

Mr. Segal and Mr. Allen felt that the entry of regulated firms would enhance competition and lower the cost of services in the industry. Mr. Segal and Mr. Allen both made reference to the ability of Congress to propose legislative remedies if abuses should occur, and Mr. Segal felt that existing laws contained adequate protection against anticompetitive practices.

ADAPSO expressed concern that the entry of banks into the data processing market would undermine competition in the industry by cross-subsidization of unregulated data processing subsidiaries by the profits from the banks' regulated activities. Voluntary tie-ins were also criticized by ADAPSO counsel P. Michael Nugent:

"Businesses seeking lines of credit with a bank receive direct and indirect pressure or suggestion from banks to bring their computer service business (such as payroll or accounts receivable/payable) to the bank. These credit applicants, hoping to curry the favor of the bank representative, often agree to have the bank serve their data processing and transmission needs. The result is lost business to the independent computer service vendor and purchase of computer services not on the basis of price, quality, or need, but as a consequence of the 'voluntary' tie-in. As such, the adverse economic effect of the voluntary tie-in is tantamount to that of the coercive tie-in. In the same way, businesses not directly involved in credit negotiations nonetheless seek to obtain preferred and hopefully guaranteed access to the scarce and 'tight' financial resources of banks and holding companies by giving the bank or holding companies their data processing and transmission business."

ADAPSO favored a remedy of permitting no competition between regulated and non-regulated companies. ADAPSO felt that if competition between regulated and non-regulated companies could not be stopped, that the regulated company should "separate the resulted and unregulated activities, so that the abuses (ADAPSO) described, such as voluntary tie-ins and cross-subsidization, don't occur as a result of spillovers of regulated economic power." Mr. Segal also favored maximum separation, but not a ban on regulated firms in unregulated industries.

Mr. Jack Biddle of the Computer and Communication Industry Association also had doubts about the entry of regulated firms into the industry, objecting to both the entry of banks and of A.T. & T., who, as a regulated monopoly can take profits derived from the regulated side of the business and flow them to the competitive side. Mr. Biddle was skeptical of maximum separation, because "as long as you have single control and ownership and flow through comes from the regulated industry to the unregulated, the incentives are to maximize the profit of the separate subsidiary." Charles Johnson, of the Independent Data Communication Manufacturers Association, similarly felt A.T. & T. would have an unfair advantage in the computer and data processing industry, stating:

"Because independently manufactured equipment must be compatible with A.T. & T.'s switched network, A.T. & T. has the power to establish de facto technical standards for that equipment. Since it governs the establishment of these standards, and the timing of their introduction into the network, A.T. & T. has the ability to deter the connection of independently manufactured equipment to its switched network, until its integrated manufacturing facility, Western Electric, can develop equipment to meet the changed or new standards."

CONRAIL CHANGES AND THEIR IMPACT ON SMALL BUSINESS

Background

Since Conrail's formation in 1976, the railroad has failed to produce a positive cash flow. In the process, Conrail has used nearly $3.3 billion of Federal funds. Unless significant changes occur, such a monetary trend will continue.

The Staggers Rail Act of 1981 mandates reports to Congress from Conrail, United States Railway Association, and the Federal Railroad Administration on needed changes and the direction Conrail should proceed in the coming years. Any changes in Conrail would affect many small businesses in a five State area that are currently dependent on Conrail service. Many of these businesses are located along short-line connections, many of which are relatively low-volume lines. These small businesses will have to find alternate rail or truck transportation if Conrail abandons service on their lines. If many small businesses go out of business as a result of increased transportation costs, it will have a significant harmful impact on their communities.

Summary of testimony

The subcommittee held hearings on June 9 and June 11, 1981, in Washington, D.C., to determine what effect the proposed Conrail changes would have on small business and small shippers. Witnesses who appeared and testified on June 9 include: Federal Railroad Administration, by Richard Schiefelbein, Deputy Administrator; Consolidated Rail Corporation, by Stanley Crane, Chairman; Ohio Rail Transportation Authority, by Robert Casey, Executive Director; and New York State Department of Transportation, by John Mladinov, Deputy Commissioner.

Witnesses who appeared and testified on June 11 include: United States Railway Association, by Stephen Berger, Chairman; Pittsburgh and Lake Erie Railroad, by Henry Allyn, Jr., President; Delaware and Hudson Railroad, by Dent Shoemaker, President; The Tamarkin Co., by Burt Tamarkin; International Boiler Works, by Fred Taylor, President; Milazzo Industries, by Samuel Milazzo; Derkshire County Shippers Association, by Thomas Lawlor.

Mr. Casey and Mr. Mladinov felt that service to the small businesses on short-line service must continue for the well being of local and State economies, regardless of whether Conrail, some other large railway, or locally owned and operated short-line operators, provide the service. They raised objections to proposed State contributions to aid Conrail.

Mr. Crane and Mr. Schiefelbein agreed that a continued temporary Federal commitment to Conrail was necessary to bring them to profitability. Mr. Crane felt that Conrail could indeed become profitable within five years. Mr. Crane and Mr. Schiefelbein agreed that Government funding for Conrail meant uncertainty. Businesses could not plan ahead as long as the status of their rail connections were in question. During the years since 1976, Mr. Crane noted, the companies that could easily switch to trucks from railroads did so, meaning that the customers Conrail currently has are likely to be more reliant on rail transport than Conrail's customers of 5 years ago.

Mr. Berger testified that the United States Railway Association recommends that a process be put into place to allow Conrail to survive if it made real economic progress. However, Mr. Berger noted, Conrail's viability depends on the willingness of labor, management, shippers, States, local governments, and other railroads to make the concessions and agreements necessary to keep Conrail alive. Attempting to transfer major portions of Conrail's lines depends on the willingness of other railroads to acquire those lines. Mr. Berger testified that there was both little interest in acquiring Conrail lines among other railroads, and little economic necessity to take an active interest in acquiring those lines, since Conrail's traffic predominately originates and terminates in Conrail's service region.

Mr. Allyn of the Pittsburgh & Lake Erie Railroad endorsed the Reagan administration's proposal to promote the transfer of Conrail's lines to the private sector within a specific time frame. Mr. Allyn expressed Pittsburgh & Lake Erie's willingness to acquire a part of Conrail's lines if the administration proposal passes Congress. Mr. Shoemaker of the Delaware & Hudson Railroad expressed opposition to Conrail's attempt to take over Delaware & Hudson's lines as part of Conrail's attempt to become profitable. A takeover of Delaware & Hudson by Conrail would be injurious to competition in Northeast rail service.

The Subcommittee heard from a small shippers panel who testified of the necessity to preserve rail service for their businesses, and of their desire to see an orderly transfer of Conrail lines to the private sector.

EPA PROPOSED RULEMAKING ON CHLOROFLUOROCARBONS AND ITS IMPACT ON SMALL BUSINESS

Background

In October 1980, the Environmental Protection Agency issued an Advanced Notice of Proposed Rulemaking restricting the production and use of nonaerosol chlorofluorocarbons (CFC's). Developed in the 1930's, CFC's are synthetic compounds that are used extensively in refrigerants and insulation.

The EPA took this action based on the theory that CFC's, released into the atmosphere, would make their way to the stratosphere and cause a reduction in the earth's ozone layer.

CFC's are widely used in the air-conditioning, automobile, food, and packaging industries. Any regulation of this substance would admittedly have an impact on the large number of small businesses within, and related to, those industries.

In conjunction with the Subcommittee hearings, Congressman Thomas A. Luken, Chairman of the Subcommittee, introduced H.R. 1853 which would prevent EPA from enacting a regulation limiting production of CFC's until it can be shown that this substance does in fact deplete the atmosphere's ozone layer.

To date, EPA has taken no action beyond the Advanced Notice of Proposed Rulemaking (ANPR).

Summary of testimony

The Subcommittee held a hearing on EPA's ANPR in Washington, D.C., on July 15, 1981, to hear testimony from small business users of CFC's, and the EPA. The witnesses who appeared were: Jon M. Pierce, P. W. Ravanesi, Timothy J. Fahrney, and John H. Reilly, representing the air-conditioning industry; H. W. "Ace" Bradley, William Jelin, Herbert Coon, Jr., and Linda Kohler, representing the foam industry; Raymond Way, John Randazzo, Glen C. Rager, David N. Freedman, and Charles Ruzzuto, representing the food industry; David Begin, a solvent manufacturer; Clay Smith, a coal cleaning processor; and Edward A. Klein of EPA.

Mr. Klein of the Environmental Protection Agency testified that the agency's concern for CFC's effect on health and environment was triggered when it was found that there was a significant increase in the use of nonaerosol CFC's during the years 1974–79. Expected recovery of the automobile and construction industries, combined with expected market growth in the use of CFC solvents, food freezing, and other applications may lead to a 5-percent annual growth rate and an eventual increase to record production levels.

Mr. Klein's testimony was based on an EPA-commissioned study of the economic implications of regulating CFC emissions from nonaerosol applications conducted by the Rand Corporation. The study concluded that a production restriction would be more effective and efficient way of curbing CFC releases into the atmosphere. The study found that production restrictions would cause the price of CFC's to rise and provide an economic incentive for firms to reduce CFC emissions, conserve CFC use, or find alternatives to CFC.

In analyzing individual industry sectors that use CFC's, the study found that the air-conditioning and refrigeration industry had no alternative to CFC's and that that industry would have to continue using and purchasing CFC's even as the prices increased. It is believed that the flexible foam industry could implement recovery and recycling technologies and could switch to substitute chemicals but it is acknowledged that the cost of recovery and recycling equipment does not appear to vary significantly with the size of the plant, thereby leaving smaller plants at a cost disadvantage. Further, it was anticipated that the foam packaging industry would be severely affected by a production restriction. It was noted that purchasers of foam packaging would likely switch to other types of packaging rather than pay the higher costs brought about by less CFC's.

The industry witnesses were unanimously opposed to production restrictions on CFC's. It was pointed out that a very large portion of the producers and users of CFC's were small businesses, often family owned and operated businesses, and they would be the most affected by any regulation enacted by EPA.

First, it was admitted that EPA was correct in projecting a price increase for CFC's if curbs are placed on the solvent's production. Small businesses universally worried, however, that they would be shut out of the CFC market because they would not be able to pay the increasing costs of the solvent. Nor did they have any hope of outbidding their larger competitors for the limited amount of CFC's that would be available.

It was further pointed out that while CFC's provide the most energy efficient method of insulating, the arithmetic of energy saving would not tolerate an increased cost of insulation. It will once again become more economical for people to waste energy.

The industry witnesses also expressed a grave concern over the lack of practical substitutes for CFC's. In the insulation industry, it was noted that CFC's provide the highest degree of energy conservation. In the foam packaging industry, witnesses testified that the substitute, pentane, is an explosive, volatile substance that poses a threat to life and property. Witnesses representing the food industry stated that CFC's are needed to manufacture the only fumigant available that eliminates bacteria from spices, and that the only alternative to preserving perishable foods, whether at the wholesale, processing, or detail level, is ammonia which is highly toxic, explosive, and flammable.

In addition, every witness, representing every industry, testified that the amount of money that would be required to change over the equipment in manufacturing plants, grocery stores, office buildings, laboratories, etc., to use a substitute for CFC's would be prohibitive to most concerns and would cause a large amount of bankruptcies and increased costs to consumers where the cost of conversion could be passed on.

HIGH INTEREST RATES AND THEIR IMPACT ON SMALL BUSINESS

Background

During the first year of President Reagan's administration, Congress, acceding to the administration's wishes, passed an ambitious program of tax and spending cuts which were to curb inflation, spur savings, and ultimately, lower the interest rates.

But by October 1981, the prime rate stood at 19 percent, savings and loans were offering home mortgages at 17½ percent, and the national unemployment rate was 8 percent. Housing production has reached its lowest level in nearly two decades, automobile sales were down 3 million from the last decade's best year, and interest rates accounted for about 10 percent of farm production costs.

Summary of testimony

In order to hear directly from the persons most affected by high interest rates, the Subcommittee held a series of hearings: In Cincinnati, Ohio on October 3; Youngstown, Ohio on October 5; and Omaha, Nebr. on October 8, 1981.

The Subcommittee heard from representatives of labor, the building industry, realtors, automobile dealers, small thrift institutions, and local small business associations.

Each witness testified about the effect of high interest rates on their sector of the economy, and the ripple effect throughout the economy. For example, automobile dealers stated that nationally, over 2,500 dealers had gone out of business over the last 30 months, and that in one metropolitan area alone, this resulted in a loss of over 20 percent of the jobs that dealers were responsible for.

A home builder testified that because of the skyrocketing interest, the average cost of a home that he builds has risen $25,000 in less than 4 months, and requires $4,000 more in down payment.

This has resulted in a severe financial loss for this builder, and the loss of business has caused the failure of 10 out of the 45 subcontractors and suppliers regularly used to construct the homes.

It was shown that on a national level, savings and loans lost $1.5 billion in the first six months of 1981.

Ohio realtors testified that their ranks will have declined by 25 percent in 1981 and that while new construction is expected to total 1.6 million units in 1982, this is inadequate to meet the 2 million units a year anticipated demand.

Many witnesses offered suggestions on how best to lower the interest rate. The recommendations which enjoyed the broadest support were:

(1) The President and Congress should take whatever steps are necessary to balance the Federal budget by fiscal year 1984, thereby reducing Government activity in credit markets.

(2) Appointment of a non-banking, small business person to fill the next available vacancy on the Federal Reserve Board.

(3) Elected officials, such as Congress and the President, should be made to have more influence and input into the decisions made by the Federal Reserve Board.

(4) The life of the All-Savers Certificate should be extended and additional steps should be taken to insure that the resulting savings be used to assist the housing industry.

(5) If the interest rate has not fallen substantially, and remained at that level for a period of time, the across the board 10 percent personal income tax rate cut scheduled for July 1, 1982, should be delayed or cancelled.

(6) Congress and the President should encourage the Federal Reserve Board to allow the money supply to grow at the upper range of their target rate.

(7) Congress should develop and authorize alternative methods of financing home mortgages, such as through pension funds or tax exempt revenue bonds.

(8) Large banks must be prevented from making huge loans to finance corporate mergers which do not add to the gross national product.

CAUSES OF THE INCREASE IN SMALL BUSINESS FAILURES

Background

In an attempt to strengthen the beleaguered economy, Congress in 1981 passed the largest tax cut in this Nation's history in order to promote savings and investment. Since then, the Federal Reserve Board maintained tight money supply policies which limited, as well as increased the cost of, available investment funds.

The country's economic condition was reflected in the Dun & Bradstreet figures on business failures. Their data for the first 23 weeks of 1982 showed that the number of business failures was 44.3 percent over one year ago. The 1981 figure reflects an increase of 110 percent over the 1979 statistics.

The 1982 failure rate is the highest since the failures recorded in 1933 in the midst of the Great Depression. At that time, 100 businesses out of every 10,000 failed. In 1982, the failure rate is expected to reach 90 out of every 10,000 concerns.

In addition, it was recognized that small businesses faced special problems during recessionary times. When credit is tight and interest rates are prohibitive, small businesses are frequently squeezed out of the credit market due to the unavailability or the high cost of money and therefore become unable to finance their operations.

Summary of testimony

In order to examine the causes and effects of the alarming increase in the number of business failures, the Subcommittee held a hearing in New York City on June 25, 1982. Witnesses included small business owners, attorneys specializing in insolvency proceedings, a banker, and an economist.

From their many years of experience in business, the small business owners observed that the Federal Reserve Board's policy of maintaining high interest rates is counterproductive in that it increases the Government deficit and further fuels inflation.

Witnesses agreed that small businesses were caught between opposing forces in that a company that made a decision several years ago to expand usually was required to do so with a variable rate loan, and now that the interest rate has reached 20 percent, they can no longer afford to service their debt. Couple this with the fact that the customers of these small businesses are also experiencing difficult times and are required to delay, or avoid, payment to the small businesses.

All agreed that only very few small businesses could make any profit while servicing a debt at 18–22 percent interest.

Further, it was recommended that the Federal Reserve Board establish policies to control not only inflation or interest rates, but the real interest rate as well. That is, the actual cost of money which is determined by subtracting the inflation rate from the interest rate charged on a loan. Historically, this rate has averaged between 2 and 3 percent. Witnesses believed that figure would be manageable in any well run company.

All witnesses agreed that in spite of the fact that money lenders are entitled to a profit on a transaction, all creditors should use moderation when attempting to collect from a small business in financial difficulty.

Mr. Mike Schochat, Vice President of the Chemical Bank, described the bank's program to reach out to small businesses and provide them not only with money but total financial management assistance.

In reviewing the overall economy and its effect on business failures, Raymond Dalio, an economist, cited these problems:

(1) The economy now has the highest debt as a percentage of GNP since the Depression years of the 1930's.

(2) Corporations now have the lowest ratio of assets to debts.

(3) Over 40 percent of all corporate debt is short-term.

(4) Real interest rates reached the highest level since 1929.

(5) The amount of money used to pay interest has not been this high since the Great Depression.

A number of witnesses, including the banker, economist, and attorneys, agreed that a viable solution to the problem would be to specifically target Government assistance to the economic sectors that need it the most, while pursuing long-term solutions to the economy.

X.—Subcommittee on Energy, Environment, and Safety Issues Affecting Small Business

The following is an outline of the Energy Subcommittee's activities in the 97th Congress.

H.R. 1362—Motor fuel marketing

On March 31 and April 1, 1981, the Subcommittee held hearings on H.R. 1362, the Small Business Motor Fuel Marketer Preservation Act of 1981. This legislation is derived from a similar bill, H.R. 6722, which was reported out of the Small Business Committee late in the 96th Congress.

Markup of H.R. 1362 was postponed while the Senate Judiciary Committee considered companion legislation, S. 326. The Senate bill was amended and favorably reported in 1981, but has not come to the floor yet. On March 15, 1982, the Subcommittee voted to table H.R. 1362.

Energy conservation and small business

The Subcommittee held two field hearings to study energy conservation by small business. The hearings were held on October 19, 1981, in Salem, Mass., and on March 15, 1982, in Cleveland, Ohio. Both hearings included considerable discussion of energy tax credits, which the administration had proposed eliminating but which were strongly supported by small businesses. The energy tax credits have been retained.

International energy negotiations

On October 21, 1981, the Subcommittee met in joint session with the Subcommittee on Energy Conservation and Power of the Committee on Energy and Commerce. The focus of the hearing was on the U.N. Conference on New and Renewable Energy, held in Nairobi last year, and on follow-up negotiations to provide financing through the World Bank for purchase of alternative energy technologies by less developed nations. The so-called Third World is seen by many as the most logical mass market for new energy technologies now being pioneered by smaller companies in the United States.

Pollution control financing

The Subcommittee held three hearings on the subject of pollution control financing for small businesses. The hearings were held on November 4, 1981, and March 10 and 31, 1982. All were in Washington, D.C.

These hearings clearly demonstrated the continuing need of small businesses for assistance in meeting extraordinary capital requirements related to compliance with environmental protection laws and regulations. The Small Business Administration's pollu-

tion control financing program was praised as a successful approach to solving this problem. The SBA program couples Federal Government loan guarantees with small-issue industrial development bonds issued by local governments.

By administrative actions in 1981, small issue IDBs were virtually eliminated and the SBA program was practically wiped out. Provisions in H.R. 6086/S. 1947 (pending final action in the Senate) would restore the SBA program. The Subcommittee has repeatedly conveyed to the Ways and Means Committee the importance of small-issue IDBs to small businesses faced with pollution control financing requirements.

Waste oil recovery

On February 11, 1982, the Subcommittee conducted a field hearing in New York City to examine the recycling of used motor oil. The waste oil recovery industry is composed almost exclusively of small businesses.

In late 1981, there were reports of various questionable activities in the handling of waste oil in New York, New Jersey, and Pennsylvania. Consequently, the field hearing examined not only the Federal programs regarding waste oil but also State and local enforcement activities.

The hearing revealed that budget cutbacks and administrative decisions have jeopardized several Federal programs which witnesses said are important to addressing the issue. For the past several months, the Subcommittee has worked successfully with other Committees to correct these problems through substantive legislation and the budget process. In addition, a General Accounting Office study on this subject is now being prepared for the Subcommittee.

Energy disruptions

On May 18, 1982, the Subcommittee held a hearing on the vulnerability of national energy distribution systems. The hearing confirmed that small businesses and agriculture are the elements in our economy which are most sensitive to interruptions in energy supplies, but that they also enjoy the greatest potential for energy independence. The witnesses all agreed that key elements of our several centralized energy distribution systems are vulnerable to disruption and that such disruptions should be anticipated.

This hearing has been followed up by an off-the-record briefing for Subcommittee members and by a GAO study being done at the Subcommittee's request.

H.R. 6389, H.R. 6391—Urea-formaldehyde foam

On August 4, 1982, the Subcommittee held a hearing to consider two bills which would provide low-interest SBA disaster assistance loans to homeowners seeking to remove/replace urea-formaldehyde foam insulation in their houses. The legislation also would assist small businesses that manufactured or installed UF and now seek to enter new ventures. UF foam was banned by the Consumer Product Safety Commission earlier this year.

Small business energy loans

On August 5, 1982, the Subcommittee conducted an oversight hearing to review the SBA's energy loan program. The Subcommittee was concerned by reports that only $1 million of the $25 million appropriated for this program has been spent, yet potential applicants were being told that no funds are available. SBA has agreed to work with the Subcommittee to assure that field offices obtain a better understanding of the program and that the available funds are used as Congress intended.

This hearing was supplemented by a Subcommittee staff report based upon a survey of current energy loan program participants. That report has been published as a committee print.

Gasoline marketing practices

Subcommittee Chairman Bedell is considering holding a set of investigative hearings during the post-election period to study recent developments in gasoline marketing. Significant changes have occurred in this industry, affecting tens of thousands of small businesses that market motor fuel products.

XI.—Subcommittee on Tax, Access to Equity Capital and Business Opportunities

Small business tax and capital formation issues have gone through wide gyrations since the start of the 97th Congress on January 31, 1981. During 1981, the Congress enacted the Economic Recovery Tax Act of 1981, which was the largest tax cut in the Nation's history. It is a program which will amount to a tax reduction of approximately $748.8 billion by fiscal year 1986.

Due partially to the magnitude of the tax relief provided by ERTA, the Treasury faces a projected budget deficit this year of $112 billion and a possible $200 billion deficit by 1984. This has caused the political situation to change to such an extent that in just one year after ERTA, the Administration and the Congress have accomplished a tax increase measure of approximately $98 billion.

The change in direction of the tax debate is just one example of the structural transformations which the economy is undergoing. Besides the tax policy debate, there are also major changes occurring in the financial services industry. The way in which the individuals and businesses meet their financial needs will dramatically change.

Proposed administration tax cuts and their effect on small business

On March 25, 26, and April 2, 1981, the Subcommittee conducted hearings on the administration's proposed tax program. The Reagan administration at that time proposed a 30-percent reduction in individual rates over three years and faster writeoffs of depreciable plant and equipment (the so-called 10–5–3 depreciation proposal).

Based on IRS statistics for 1975, small business does not greatly benefit from accelerated depreciation reform. For example, 92.9 percent of all firms are wholesalers, retailers, and other service sector firms. These firms are labor intensive, as opposed to capital intensive.

Various testimony did suggest that the 30 percent, three-year individual rate cut would help the many small businesses that are sole proprietors, partners and subchapter S corporations. There was concern, however, as to the equity and inflationary nature of the cuts. In addition, there were concerns raised as to the impact of the administration's program in light of the Federal Reserve Board's tight monetary policy. This latter policy must be seen in the light that smaller firms bear the brunt of high interest rates.

Given the uncertain impact of the administration's program, the purpose of the hearings was to insure that any tax package ultimately enacted by Congress would include an equitable share of relief for small business, especially labor intensive firms.

In specific, the Subcommittee focused on promoting a mix of incentives which will benefit labor and capital intensive small businesses. Some of the proposals endorsed by Chairman Nowak and other members of the Subcommittee were as follows:

(1) A further tiering of the corporate rate from $100,000 to $250,000;

(2) A small business rollover provision;

(3) An increase in the amount of used equipment eligible for the investment tax credit from $100,000 to $200,000; and

(4) Inventory accounting reform (including a provision for cash accounting and LIFO simplification).

Another aspect of the tax debate which the Subcommittee investigated in June 1981, was the impact of Federal estate and gift tax laws on small closely held businesses and family farms. The Subcommittee was concerned with the fact that large sums of money were being spent on estate planning and life insurance. It was felt that such expenditures are an unproductive use of capital, which could otherwise be used for capital formation purposes and plant expansion.

The Subcommittee's push for tax simplification of inventory accounting methods was compared to the rationale underlying depreciation reform. Both types of reform aid capital formation by increasing the internal cash flow of a business. Inventory reform, however, helps the vast majority of smaller firms which are labor and inventory intensive.

Based on the Subcommittee's investigations, the Subcommittee chairman introduced H.R. 2319, the Inventory Simplification and Reform Tax Act of 1981. The bill simplifies the tax treatment of inventories by:

(1) Repealing the LIFO conformity requirement;

(2) Simplifying the implementation of the LIFO method. For smaller firms, this involves (among other provisions) a reduction of the number of inventory pools and for the use of published price indexes;

(3) Enactment of the cash method of accounting for specified small businesses; and

(4) An objective standard in the treatment of excess or obsolete inventory.

Although the Subcommittee would have preferred having small business receive a greater share of the relative tax reduction relief provided by the Economic Recovery Tax Act (ERTA) of 1981, as signed into law by the President, many of the Subcommittee's tax proposals were conceptually included in ERTA. The Subcommittee was particularly successful in having its recommendations on estate and gift tax reform and LIFO simplification included in both ERTA and in the Ways and Means alternative tax package.

The Subcommittee is very cognizant of the current economic and budget malaise facing the Nation. This will probably serve to mitigate any realistic push for further tax and capital formation relief for small business in the near term. Nevertheless, Chairman Nowak and other Subcommittee members realize that ERTA did not provide sufficient tax relief for noncapital intensive firms. Accordingly, in terms of long range economic policy, the Subcommittee will continue to advocate for a further reduction or tiering in

the corporate rate, substantial simplification of the subchapter S provisions, a jobs tax credit (including a bonus provision to address the Nation's skilled labor shortages and its economically distressed citizens), enactment of a small business participating loan type mechanism, and for further inventory accounting simplification.

Safe harbor leasing

One of the more controversial provisions of the Economic Recovery Tax Act was found to be the safe harbor leasing provisions. These provisions were included in ERTA for the purpose of extending the new depreciation benefits to businesses which do not have current taxable income. Some commentators contend that leasing is an important vehicle for increasing the internal cash flow of capital intensive small firms.

As a result of its receiving numerous letters from small business persons regarding the complexity and general unavailability of benefit from safe harbor leasing, the Subcommittee conducted an investigatory hearing on the subject on February 25, 1982.

Hearing testimony suggested that the statute effectively precludes small businesses from becoming lessors in such transactions. There was also concern as to the impact that the so-called "at risk" tax rules will have on any leasing transactions. Others raised a fundamental economic question as to whether financial institutions will, in fact, find small leasing deals profitable.

Due in large part to its projected revenue loss, the Congress made changes in the new tax act which will reduce the leasing tax benefit. This is a result of the Joint Committee on Taxation estimates that the revenue loss associated with the provisions will total $27 billion by 1986.

Section 385: Debt-equity tax regulation

Concerned with the potential impact that the proposed section 385 "debt-equity" regulation would have on capital formation, Chairman Nowak introduced (along with the cosponsorship of all the other Small Business Subcommittee Chairmen) in May, the Small Business Regulatory Relief Tax Act (H.R. 6429). The bill delays the effective date of the regulation from July 1, 1982, to July 1, 1984. Sensing the growing support for the measure, Treasury has recently agreed to delay implementation of the regulation until April 1, 1983.

The problem with the debt-equity regulation is its complexity and its impact of the ability of smaller firms to raise and generate capital. To the extent an individual makes a loan to his business, it is possible that the regulation (as drafted) would cause the loan to be reclassified as stock. In general, this situation could result in the interest paid by the business on its loan repayments not be deductible for tax purposes. This is significant to the small businessman because such a reclassification could potentially result in a dramatic reduction in the firm's cash flow. Accordingly, the delay until April 1, 1983 will allow Congress sufficient time to analyze its impact on small business capital formation.

Job creation and the revitalization of small business

The Subcommittee on Tax conducted hearings on September 15 and 22, and October 14, 1981, to investigate the role of small business in job creation and urban revitalization. The three primary areas of discussion were: The need for viable economic incentives for distressed areas; the effectiveness of tax exempt small issue industrial bonds; and the impending skilled labor shortages facing the Nation.

The hearings were based on the premise that the future vitality and economic growth of the United States economy is dependent on small business. This premise is derived from the fact that small business is the linchpin of the job generation process and the major source of innovation in our economy.

With small business in the role of primary job creator and innovator, the Nation's economy is undergoing major structural changes. These changes are occurring both in terms of a decline in the general prosperity of the older urban centers and with respect to a change in the types of industries upon which the economy is based which represents a shift from a heavy industrial emphasis to an increasing concentration into the service industries dominated by smaller, more innovative firms.

Another important factor which must be considered in the discussion of job creation is the present Administration's shift in budgetary priorities from general domestic spending to a sharp increase in defense spending. The result of these shifts will have a major impact on the ability of the cities to provide adequate services, economic prosperity and full employment for urban residents. In addition, we will see an increase in the need to bolster our skilled labor sector to provide adequate manpower to service the growth of our military industrial base.

On the basis of all the evidence received and further investigation, the Subcommittee on Tax compiled a report entitled, "Job Creation and the Revitalization of Small Business" (Report No. 97-434) which analyzes the major areas of focus of the hearings. The brief summary of the findings and recommendations are as follows:

1. Economic incentives to distressed areas

The basis for the concept of providing targeted tax incentives and deregulation will result in an increase in business investment and job creation in the Nation's older urban centers. Although this tax relief strategy promises to provide a measure of relief for areas suffering from long-term economic deterioration, they cannot and should not be considered as a cure for all our urban problems. In essence these tax proposals should not constitute an entire program for economic development but should be viewed as an integral component of a well balanced urban revitalization scheme.

a. *Infrastructure.*—In recent years the United States has found itself facing an infrastructure crisis which is not necessarily isolated to the older urban centers of the Nation. This crisis involves the ability of localities to maintain and improve proper sewer and transit systems (streets, bridges, etc.) including community support services (police, fire, etc.). In order to encourage the business community to locate and remain in our urban centers, a locality must

provide a healthy and safe commercial environment which, at the very minimum, necessitates a viable infrastructure base.

b. *Human Capital.*—Another important area to consider in any urban development plan is a program to address the human capital needs of the community. Current Federal programs involving defense, transportation, water, air, and energy, have an important impact on economic development and job creation. In order to strengthen these programs there should be a provision designed to effectuate human capital development specifically focusing on assisting the unemployed and the underemployed by resolving the skilled labor shortage and training the unskilled with the basic aptitude to become productive workers. In this area, the focus should be on training workers so that they have the ability to fill specific positions in the private sector where there is the greatest need. In response to the realization that private sector placement should be emphasized, the Private Sector Initiative Program under Title VII of CETA was enacted in 1978, for the purpose of helping to eventually redirect CETA's emphasis on public sector employment toward private sector jobs. Under the Private Sector Initiative Program, private industry councils would be set up in communities to increase the employment and training opportunities in the private sector for the economically disadvantaged. Members of the council would be from private industry, labor, community based organizations, and local educational systems or programs. In general, these councils provide funding for private companies to defray the cost of training. It is this type of private sector oriented program that should be mentioned in any effort to implement a national employment policy.

c. *Financing.*—A crucial element of a coordinated plan of economic development is the availability of adequate financing for businesses locating in distressed areas. Although tax incentives are an important method for increasing the internal cash flow of a profitable firm and will undoubtedly encourage it to locate and expand in an urban development zone, tax benefits will provide little or no assistance to small firms which are in their start-up or early years of development. Therefore, a startup business will be forced to look elsewhere to meet its capital formation needs.

Securing adequate financing is generally more difficult for new and small firms than for established larger firms who are able to utilize tax benefits as well as alternative sources of financing such as the securities and commercial paper markets. To a large degree, new small businesses rely heavily on personal savings or personal loans from family and friends for their financing needs. In addition, high and volatile interest rates have rendered commercial financing unaffordable to many small businesses.

Therefore, to augment the tax incentive provisions of a distressed area proposal, there must be measures included which will provide firms (especially start-ups) or investors with funds for seed or working capital from external sources such as loans or grants.

d. *Tax Incentives.*—Tax incentives are an important element in the dynamics of job creation and the revitalization of distressed areas. In particular, targeted tax incentives are an important supplement to the human capital, infrastructure and seed capital needs of a local community. To the extent, therefore, that tax in-

centives are included in a well balanced plan for economic development, it must be understood that many tax benefits do not have the same impact on the cash flow of all types of businesses equally. This necessitates a distinction between those tax incentives which meet the capital formation needs of labor intensive small firms and those which meet the needs of capital intensive firms such as manufacturers.

The Subcommittee, therefore, found that a jobs' tax credit would be particularly beneficial to labor intensive firms in urban areas. In addition, an accelerated depreciation or direct expensing provision (including investment tax credit relief) would greatly aid the cash flow needs of capital intensive firms. Recognizing the limited amount of capital that small firms have at their disposal, the current limit on used equipment eligible for the investment tax credit is discriminatory against the small business person and should be raised.

Further, the Subcommittee found that a small business participating loan mechanism promises to offer a measure of relief for small businesses from their capital formation burdens.

In addition, the following tax reduction measures or proposals would be viable incentives for fostering economic development: The rehabilitation investment tax credit; a credit to offset a portion of the interest earned by a lender on a loan; and a provision encouraging the use of Employee Stock Ownership Plans (ESOPs) which could act as an inducement to increase the productivity of workers in distressed areas.

2. Tax exempt small issue industrial development bonds

In view of the widespread criticism concerning the industrial development bond (IDB) program, many opponents including the administration, have pushed for restrictions on the use of tax exempt small issue IDBs.

In analyzing the use of small issue IDBs, the Subcommittee concluded that small issues are an important economic development tool which can be utilized by States and local governments to stimulate business investment and employment. IDBs become an especially critical source of capital and means of economic development due to the fact that the vast majority of Federal economic development programs have been designated as prime targets for budgetary cutbacks. In particular, IDBs may be one of the few sources of low cost capital for small firms who are being eliminated from conventional financing by high and volatile interest rates.

3. Skilled labor shortage

The current high level of unemployment demonstrates a strange dichotomy in our Nation's employment base when measured against the acute shortage of skilled workers, which is attributable, in large degree, to the use of automation and technology. Employers, especially small business persons, often do not have the time or the capital to train employees to fill the deficiency of skilled workers. These critical shortages have contributed to the country's declining productivity, may undermine our position in world trade and may have a significant impact on our national defense capabilities.

Two possibilities for alleviating this problem are a specialized skills training tax credit for the specific industries facing a demonstrable shortage of skilled labor and a coordinated jobs training program utilizing input from the Government, education, and industry sectors of the community.

Impact of high interest rates on small business capital formation

On October 15, 1981 and February 24, 1982, the Subcommittee held hearings to study the impact of interest rates on small business capital formation.

The Administration's plan for economic recovery includes tax cuts and budget cuts while the Federal Reserve Board strives for restrictive monetary targets to curb inflation. In the midst of these economic policies, the burden of high and volatile interest rates is rendering the prospects of an investment led economic resurgence extremely unlikely.

There is widespread disagreement among economists, financial analysts, and others over the exact cause of the protracted high level of the interest rates. The most frequently mentioned reasons for the persistent high interest rates have been the Federal Reserve Board's tight monetary policy, the demand for credit by the Treasury due to the huge projected Federal deficits, and the inflationary expectations of the financial markets.

Although there may be a mystery relative to the cause of the high interest rates, there is little doubt as to their effect, which has resulted in prolonged economic stagnation marked by declining productivity, decreased sales and mounting inventories, rising business failures, and record level unemployment.

Nowhere in the economic spectrum has the prohibitive nature of these high rates been felt more than on the small business community. Small firms have traditionally relied almost exclusively on conventional credit as a source of outside financing. However, the current rates of interest have rendered this major source of funds virtually unavailable to the small business person.

It is true that our country is presently facing an economic crisis in which we must all share the burden of economic restraints. However, we cannot follow an economic course which threatens to irreparably harm the small business community, the cornerstone of the Nation's growth and vitality.

The devastating impact of these interest rates on the economy in general and small business specifically have pushed the small business community and others to demand that some immediate action be taken to ease their burdens. Evidence of this urgency was expressed by hearing witnesses who claim that there is growing support for urging the Federal Reserve Board to allow a modest increase in money growth to bring the interest rates down to a workable level. This action, they claim, would be the spur to economic recovery without subjecting the country to runaway inflation.

Small Business Venture Capital Act of 1981

The Subcommittee held a hearing on March 24, 1982, on H.R. 5302, the Small Business Venture Capital Act of 1981. Chairman Nowak introduced the measure with Representative Dan Marriott, the Ranking Minority Member, to encourage greater utilization of

the SBIC program as an important source of funding of venture capital for the small business community.

H.R. 5302 removes unnecessary limitations on the amount of leverage available to any one SBIC and will permit the SBICs to include a restricted portion of the unrealized appeciation of their marketable securities for leveraging purposes. The bill also eliminates the overlapping and dual regulation of certain SBICs which are subject to both the Investment Company Act of 1940 and the Small Business Investment Act of 1958.

Since 1958, when Congress recognized the need to develop an organized source of venture capital for the small firms, the SBIC program has displayed an exceptionally successful track record. For example, recent SBA statistics indicate that approximately 47,000 small companies have received over $4 billion in venture capital investment as well as invaluable management assistance since the establishment of the SBIC program.

A recent study demonstrates the cost efficiency of the SBIC program. According to this study, the Government spent only $4 million on the SBIC program in 1979. This Federal outlay appears slight when measured against the fact that the SBICs or portfolio companies and their employees paid over $440 million in Federal taxes in that same year. The breakdown of these statistics indicates that the Government has received more than $110 in tax revenues for every dollar spent in this program.

Greater utilization of the SBIC program is one important way of dealing with the current recessionary trends in the economy. In particular, it is one of the best incentives for spurring growth and expansion of small business in the creation of new jobs.

Bank deregulation and its impact on small business lending

On May 19 and 20, 1982, the Subcommittee held hearings to investigate the current status of proposed banking deregulation and its impact on small business lending.

Recent developments in the financial service business and proposed measures to deregulate the banking industry could have a profound effect on the basic structure of the traditional lending practices in this country. In view of this trend, it is important to examine the effect of these changes on the availability of credit to the small business community.

As a general rule, small business is experiencing difficulty in securing debt and equity capital. For instance, small firms, to a large degree, have been denied access to the bond market and the commercial paper market which are significant sources of debt capital for larger enterprises. Therefore, small business has consistently relied on commercial bank credit to meet its financing needs. In fact, a recent survey by the Interagency Task Force on Small Business Finance indicates that commercial banks believe thet they provide 72 percent of all small business total indebtedness. In addition, the same survey points out "small and medium-sized banks provide the bulk of the dollar volume of bank loans to small business."

Since the small business community is heavily dependent on bank financing, changes in the basic structure of financial services could have a profound effect on the small business capital forma-

tion process. It is important, therefore, to examine briefly some of the recent developments in the financial service industry.

The current high and volatile interest rates have left thrift institutions on the verge of total collapse, as evidenced by a recent report in *Nation's Business*, which claims that savings and loan institutions losses totaled $5 billion last year and mergers are responsible for the elimination of approximately one savings and loan a day. The basic reason for the decline of the savings and loans is that they are being forced to pay more for funds that they are receiving from their long-term, low-yield mortgage portfolios, many of which were negotiated prior to the advent of flexible mortgage instruments.

Commercial banks are also experiencing difficulties which are partly attributable to the current high interest rates, since Regulation Q limits the amount of interest that can be paid by insured commercial banks, mutual saving and savings and loan associations. Although Congress has responded to this problem through the Depository Institutions Deregulation and Monetary Control Act of 1980, which establishes a committee to effectuate a gradual phase out of the interest rates ceiling, commercial banks continue to receive competitive pressure from such creative financial instruments as Money Market Mutual Funds.

Money Market Mutual Funds could be the greatest source of financial drain on the banking industry's resources. During times of high interest rates and high inflation, consumers are searching for ways to get the greatest return on their savings dollars. Although banks and savings and loans can now offer higher interest rates on some long-term instruments, money market funds may still be more attractive to customers because they offer a high yield plus a greater degree of liquidity.

Another major threat to the financial position of many banks is the rise of the financial service supermarkets such as Sears, American Express, and Merrill Lynch. Basically, these unregulated financial service operations, in addition to being able to provide customers with a high return and flexibility on their investment, are able to provide the customer with the convenience of a vast array of investment services.

On the other hand, banks are barred from certain markets and products by Federal regulation.

Even the banking industry itself is sharply divided on the issue of bank deregulation. Many large banks, for example, would advocate the total deregulation, letting the competitive free market determine the survival of these institutions. However, many small and medium-sized banks argue that total deregulation could lead to obliteration of local community based banks through merger and acquisition, thereby eliminating a major source of financing for farmers, small businesses, and local customers.

In addition, it should be noted that the function of these hearings was not to advocate a position for or against deregulation of the banking industry, but to investigate the future availability of adequate financing for the small business community under a regulated or deregulated banking industry scenario.

Some of the more significant recommendations presented by witnesses at the hearings are as follows:

(1) In order to sufficiently assess small business financing activity and needs, a statistical data base should be developed to collect information on the flow of funds to small business so that it is possible to effectively monitor the impact of competition and deregulation in the upcoming years.

(2) An organized regulatory environment should be developed for the financial service industry and that regulation should be even handed across all segments of the industry.

(3) Although many commentators contend that existing antitrust laws are sufficient to monitor any anticompetitive practices which may occur in the financial service industry as a result of deregulation, especially with regard to the liberalization of nationwide branching, there should be additional safeguards designed to complement the existing antitrust laws, These safeguards should include limits on regions or product markets to be entered, or limits on the size of the market share of banks which might be acquired.

Tax incentives and small business exports

On September 16, 1982, the Subcommittee conducted a hearing on Tax Incentives and Small Business Exports to investigate the utilization by small business of the so-called domestic international sales corporation (DISC) tax incentive and to explore the underlying rationale for providing tax incentives for exports generally.

For purposes of the Internal Revenue Code, a DISC is a domestic corporation which generally derives 95 percent of its gross receipts from export related activities and has 95 percent of its assets involved in exporting. Those DISCs that increase export sales over a base period amount are generally permitted to defer the tax on 50 percent of export income. With respect to the economic impact of these provisions, there were 7,208 active DISCs in 1979 with total export gross receipts of $99.6 billion.

Witnesses were encouraged by the potential impact that increased exporting could have on the growth of our workforce. This is significant in the light that small business creates about 80 percent of all the net new jobs in the United States. Further by fostering the exports of small business, the Nation will be utilizing an important avenue for broadening its economic base. It would provide our cities with a hedge against general downturns in the economy, as well as a vehicle for increasing business opportunities for other domestic industries and suppliers.

The Reagan administration and Congress should closely analyze the current market forces existing in international trade. We must stand ready to provide American firms and small business, in particular, with the proper tools to compete in world markets.

With respect to the simmering debate over the modification or replacement of DISC, two points stand out: First, we must work towards the objective of providing incentives that truly increase our level of exports abroad and which create jobs at home. Second, we must recognize that small and medium sized firms have a critical stake in this debate.

XII.—Subcommittee on Export Opportunities and Special Small Business Problems

1. Oversight of the Regulatory Flexibility Act

The Subcommittee has held several hearings to determine whether or not Federal agencies have been adhering to the requirements of the Reg Flex Act of 1980. On September 22, the Subcommittee held its final hearing on the subject. In particular, the Subcommittee will focus on the non-compliance of the Department of Defense and the Internal Revenue Service.

After the hearings have concluded the Subcommittee will issue a report with recommendations on possible improvements to the act.

2. Federal assistance to small business

The Subcommittee has held several hearings to determine what various Federal agencies are doing for small business. These hearings concluded in September.

3. Federal procurement of food products

The Subcommittee held five days of hearings on the food procurement practices of the Department of Agriculture focusing on the school lunch program. A report will be issued prior to the end of the Congress.

4. Exports

The Subcommittee has been working with the various Federal agencies which affect exports to promote more small business participation in the export area. On September 21, the Subcommittee will hold an all-encompassing hearing on the subject. The hearing will be a culmination of a six-month long series of hearings held across the Nation by the Chamber of Commerce of the United States.

A field hearing on the subject will be held on October 1 in Toledo, Ohio.

5. Other issues

The Subcommittee has been involved in several other issues in recent months which include:

(a) The continued effort by the Federal Trade Commission to regulate the funeral industry;

(b) Efforts to increase Federal competition with small business contained in the Defense Authorization bills;

(c) Oversight of Federal regulations governing the Prompt Payment Act of 1981;

(d) An attempt by the IRS to exempt itself from the Paperwork Reduction Act of 1980; and

(e) Attempts by several agencies to exempt themselves from both the Regulatory Flexibility Act of 1980 and the Paperwork Reduction Act of 1980.

(f) The Subcomittee's chairman announced that the Postal Service will issue a commemorative envelope for small business in 1984.

(g) The Subcommittee chairman served as vice-chairman of the Florida Governor's Conference on Small Business.

XIII.—Hearings and Meetings Held by the Committee on Small Business and Subcommittees, 97th Congress

Full Committee:

February 23, 1981—Meeting on "Small Business Issues with Various Trade Association Representatives."

March 12, 1981—Meeting on "Views and Estimates on SBA's Budget."

March 18, 1981—Hearing on "Budget Recommendations."

March 18, 1981—Meeting on "Views and Estimates on SBA's Budget."

April 7, 1981—Hearing on "The Effect of the Federal Monetary Policy on the Small Business Community."

April 29, 1981—Hearing on "Small Business and Minority Problems." (Joint hearing with the Subcommittee on Labor Standards of the Committee on Education and Labor.)

June 2, 1981—Markup of H.R. 2998—Loan Consolidation and Improvement Act of 1981, ordered reported.

June 9, 1981—Markup of Budget Reconciliation, ordered reported.

July 7, 1981—Hearing on "Small Business Issues." (Los Angeles, Calif.)

July 18, 1981—Hearing on "Small Business Issues." (Chicago, Ill.)

September 1, 1981—Hearing on "Small Business Issues." (Phoenix, Ariz.)

September 16, 1981—Meeting on "Small Business Issues with Various Trade Association Representatives."

October 6, 1981—Markup of H.R. 4500—SBA 8(a) Pilot Program, ordered reported.

October 22, 1981—Markup of H.R. 4326—Small Business Innovation Development Act of 1981, ordered reported.

January 18, 1982—Hearing on "Small Business Issues." (Atlanta, Ga.)

March 2, 1982—Hearing on "SBA Budget."

March 9, 1982—Hearing on "SBA Budget."

March 15, 1982—Hearing on "Small Business Issues." (Philadelphia, Pa.)

April 8, 1982—Hearing on "Disaster Programs." (San Francisco and Santa Cruz, Calif.)

May 4, 1982—Hearing on "Innovation."

May 11, 1982—Markup of H.R. 6086—1982 Omnibus Bill, ordered reported.

May 18, 1982—Markup of H.R. 4326—Small Business Innovation and Research Development Act of 1981, ordered reported.

Subcommittees:

SBA AND SBIC AUTHORITY, MINORITY ENTERPRISE AND GENERAL SMALL BUSINESS PROBLEMS

April 7, 1981—Hearing on "SBA Legislation."
May 19, 1981—Markup of H.R. 2998—Loan Consolidation and Improvement Act of 1981, ordered reported.
May 21, 1981—Hearing on "SBA 8(a) Program."
June 3, 1981—Hearing on "H.R. 2997—SBA's Disaster Loan Program."
June 4, 1981—Hearing on "SBA's 8(a) Program."
June 10, 1981—Hearing on "SBA's 8(a) Program."
September 22, 1981—Hearing on "SBA's 8(a) Pilot Program."
September 23, 1981—Hearing on "Cable Television Industry."
September 28, 1981—Meeting on "H.R. 4500, SBA's 8(a) Pilot Program."
October 13, 1981—Hearing on "Cable TV Industry-Small Business Participation."
November 4, 1981—Hearing on "Cable TV Industry-Small Business Participation."
November 12, 1981—Hearing on "Outer Continental Shelf Leasing Activities."
February 25, 1982—Hearing on "Administration's Budget Request for Small Business Administration."
April 28, 1982—Hearing on "Pending SBA Legislation."
April 29, 1982—Hearing on "Pending SBA Legislation."
May 5, 1982—Hearing on "H.R. 5022, the Small Business Contract Payment Procedures Act."
May 6, 1982—Markup of H.R. 6086—1982 Omnibus Bill.
June 16, 1982—Hearing on "SBA's Small and Minority Enterprise Development Programs."

GENERAL OVERSIGHT

May 19, 1981—Hearing on "Impact of the Reagan Administration's Economic Policies on America's Small Businesses."
June 18, 1981—Hearing on "Government Procurement."
June 23, 1981—Hearing on "Government Procurement."
June 25, 1981—Hearing on "Government Procurement."
July 30, 1981—Hearing on "Impact of Prime Rate on SBA Loans."
September 15, 1981—Hearing on "Innovation."
September 21, 1981—Hearing on "Investigation of Insurance Agents' Commissions."
October 7, 1981—Markup of H.R. 4326—Small Business Innovation Development Act of 1981, ordered reported.
February 18, 1982—Hearing on "Worker Compensation Rate-Setting Reform."
March 23, 1982—Hearing on "Productivity."
March 24, 1982—Hearing on "Productivity."
March 31, 1982—Hearing on "SBA Guaranteed Loans."
June 23, 1982—Hearing on "Business Failure Epidemic."
July 28, 1982—Hearing on "SBA's Section 503 Certified Development Company Program."

ANTITRUST AND RESTRAINT OF TRADE ACTIVITIES AFFECTING SMALL BUSINESS

May 7, 1981—Hearing on "Computer and Data Processing Industries."

June 9, 1981—Hearing on "Proposed Conrail Changes and Their Impact on Small Business."

June 11, 1981—Hearing on "Proposed Conrail Changes and Their Impact on Small Business."

July 15, 1981—Hearing on "EPA Regulations of Chlorofluorocarbons."

October 3, 1981—Hearing on "High Interest Rates and Their Impact on Small Business." (Cincinnati, Ohio.)

October 5, 1981—Hearing on "High Interest Rates and Their Impact on Small Business." (Youngstown, Ohio.)

October 8, 1981—Hearing on "High Interest Rates and Their Impact on Small Business." (Omaha, Nebr.)

June 25, 1982—Hearing on "Small Business Failures." (New York, N.Y.)

September 9, 1982—Hearing on "Impact of Federal Antitrust Enforcement Policies on Small Business."

ENERGY, ENVIRONMENT, AND SAFETY ISSUES AFFECTING SMALL BUSINESS

March 31, 1981—Hearing on "Gasoline Marketing Practices."

April 1, 1981—Hearing on "H.R. 1362, Small Business Motor Fuel Marketer Preservation Act of 1981."

October 19, 1981—Hearing on "Energy Conservation by Small Business." (Salem, Mass.)

October 21, 1981—Hearing on "The U.N. Energy Conference and Energy in Developing Countries." (Joint hearing with the Subcommittee on Energy Conservation and Power of the Committee on Energy and Commerce.)

November 4, 1981—Hearing on "Pollution Control Financing for Small Business."

February 11, 1982—Hearing on "Waste Oil Recovery." (New York, N.Y.)

March 10, 1982—Hearing on "Pollution Control Financing for Small Business."

March 15, 1982—Hearing on "Energy Costs."

March 16, 1982—Markup of H.R. 1362—Small Business Motor Fuel Marketer Preservation Act of 1981.

March 31, 1982—Hearing on "Pollution Control Financing for Small Business."

May 18, 1982—Hearing on "Vulnerability of Energy Distribution Systems."

August 4, 1982—Hearing on "Urea-Formaldehyde Foam Insulation."

August 5, 1982—Hearing on "Urea-Formaldehyde Foam Insulation."

TAX, ACCESS TO EQUITY CAPITAL AND BUSINESS OPPORTUNITIES

March 25, 1981—Hearing on "President Reagan's Economic Program."

March 26, 1981—Hearing on "President Reagan's Economic Program."

April 2, 1981—Hearing on "The Tax Reduction Portion of the Administration's Economic Program and Its Effect on Smaller Firms."

June 16, 1981—Hearings on "Estate and Gift Taxes as They Affect Small Business."

June 17, 1981—Hearing on "Estate and Gift Taxes as They Affect Small Business."

September 15, 1981—Hearing on "Job Creation and Revitalization of Small Business."

September 22, 1981—Hearing on "Job Creation and Revitalization of Small Business."

October 14, 1981—Hearing on "Small Business Industrial Development Bonds."

October 15, 1981—Hearing on "The Impact of High Interest Rates on Small Business Capital Formation."

February 24, 1982—Hearing on "The Impact of High Interest Rates on Small Business Capital Formation."

February 25, 1982—Hearing on "Safe Harbor Leasing."

March 24, 1982—Hearing on "Venture Capital Act."

May 19, 1982—Hearing on "Bank Deregulation and Its Impact on Small Business Lending."

May 20, 1981—Hearing on "Bank Deregulation and Its Impact on Small Business Lending."

September 16, 1982—Hearing on "Tax Incentives and Small Business Exports."

EXPORT OPPORTUNITIES AND SPECIAL SMALL BUSINESS PROBLEMS

April 28, 1981—Hearing on "The Role of Small Business in the USDA's Commodity Procurement Process."

April 29, 1981—Hearing on "The Role of Small Business in the USDA's Commodity Procurement Process."

May 13, 1981—Hearing on "The Role of Small Business in the USDA's Commodity Procurement Process."

July 15, 1981—Hearing on "The Role of Small Business in the USDA's Commodity Procurement Process."

July 16, 1981—Hearing on "The Role of Small Business in the USDA's Commodity Procurement Process."

September 22, 1981—Hearing on "Federal Assistance to Small Business."

September 23, 1981—Hearing on "Federal Assistance to Small Business."

September 30, 1981—Hearing on "Independent Trucker Training Conferences."

October 7, 1981—Hearing on "Regulatory Flexibility Act."

October 20, 1981—Hearing on "Regulatory Flexibility Act."

October 21, 1981—Hearing on "Regulatory Flexibility Act."

April 1, 1982—Hearing on "Regulatory Flexibility Act."

July 27, 1982—Hearing on "FAA Regulatory Flexibility."

August 18, 1982—Hearing on "FAA Regulatory Flexibility."

September 21, 1982—Hearing on "Export Promotion and Small Business."

September 22, 1982—Hearing on "Regulatory Flexibility Act."

September 22, 1982—Hearing on "Federal Assistance to Small Business."

○